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DGAP ANALYSIS

The G7's Geoeconomic Future

Insights from Conflicts with Russia, China, and Iran

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In an increasingly conflictual global environment, the G7 has become a more and more important geoeconomic actor. Yet looking at the case studies of Russia, Iran, and China reveals that the geoeconomic role the G7 plays has been mixed. For the G7 countries to improve their geoeconomic impact, they need to align their interests and risk perceptions, as well as improve their ability to propose and enact geoeconomic measures. In addition, the G7 should bolster its partnerships with other democracies and like-minded countries.

– **G7 members often employ geoeconomic strategies to advance national economic and security interests.**

– **The G7 does not utilize its full geoeconomic potential because of its informal institutional set up, the different capacities of G7 countries for deploying geoeconomic tools, and risk perceptions and interests that are not always aligned among its member states.**

– **The G7 needs new and expanded working groups reflecting a growing agenda that includes financial stabilization, sanctions coordination, and defense.**

– **The G7 should bolster its partnerships with like-minded countries by inviting them to participate in issue-specific working groups, investment initiatives, and political declarations.**

Executive Summary

The G7 is confronted with a rapidly changing geopolitical and geoeconomic environment. Russia's large-scale invasion of Ukraine in 2022 marks a turning point in international relations and the global economy. In addition, rivalries between Western democracies and autocratic regimes, especially between the United States and China, are intensifying. In this geoeconomic environment, the role of the G7 – a club of economically powerful nations that also stands for democracy, rule of law, respect for human rights, and the free market – is once again growing in importance.

But how strong and sustainable is this new geoeconomic alignment of G7 countries? After laying the groundwork by defining geoeconomics – also in the context of the G7 – three case studies will analyze the successes and failure of the joint geoeconomic commitments and policies of the G7. The period of analysis ends in December 2023.

CASE STUDY 1 RUSSIA

Russia was officially admitted to the G7 in 1998. However, after the annexation of Crimea in 2014, the G7 suspended Russia's membership "until Russia changes course." (The meetings of the G7 from 1998 to 2013 that included Russia were known as the G8.) With the invasion of Ukraine in 2022, the G7 immediately reacted in a united and assertive way, imposing export controls and sanctions. However, G7 countries neither succeeded in destroying Russia's war economy nor in changing Russia's determination to continue with its military assault on Ukraine. In addition, the G7 are not big enough to truly prevent Russian oil sales to the Global South and other countries. Changes in strategy will likely not come through economic warfare (sanctions and export controls), but through military victories and the delivery of modern weapons and ammunition to Ukraine.

CASE STUDY 2 IRAN

Conflicts between the Islamic Republic of Iran and members of the international community have persisted for nearly five decades and involved disputes across a range of issues. Recent flash points include the Russian use of Iranian-designed Shaheed drones, Iran's alleged support for the October 7, 2023, attacks on Israel, and Iran's support for the Houthis' attacks on Red Sea shipping. Since the withdrawal of the United States from the Iran nuclear agreement, formally known as the Joint Comprehensive Plan of Action (JCPOA), in 2018, the G7 has ceased operating effectively as a sanctions-coordinating body on Iran. Recent developments may, however, move the threat perceptions of European G7 members toward those of the United States, which would restore G7 unity.

CASE STUDY 3 CHINA

China has often been at odds with the United States and other liberal democracies. G7 members object to China's authoritarian government and illiberal economic system as well as its human rights violations. This has been exacerbated by the presidency of Xi Jinping, which has stoked Chinese nationalism and used Chinese economic power for coercive and destabilizing purposes – which the G7 sees as a pattern of aggressive Chinese behavior. The G7 has served as a platform for focusing attention on these concerns. Human rights issues have been addressed – albeit to negligible effect – through visa bans and asset freezes coordinated among G7 members. The most significant geoeconomic actions against China, however, have been unilateral export bans and procurement restrictions led by the United States, with G7 buy-in as a follow-on effort.

MIXED RECORD FOR THE G7 AS GEOECONOMIC ACTOR

The G7 members frequently employ geoeconomic strategies, including economic instruments, to defend and advance national economic and security interests. Yet, taking the findings of the three case studies into account, the picture for the G7 as a geoeconomic actor is mixed. There are five primary reasons for this:

1. The G7 has a limited formal institutional set up and limited tool kit. Monitoring compliance is limited, and there is no formal enforcement mechanism.

2. G7 members have different capacities for deploying geoeconomic tools.

3. While the G7 countries share many values, their economic dependencies, risk perceptions, and interests are not always aligned.

4. Even when G7 members share the same objectives, they sometimes differ in their strategies and tactics (e.g., regarding Iran).

5. The decreasing economic share of the G7 countries has and will continue to reduce the power of its geoeconomic instruments.

RECOMMENDATIONS

To improve their geoeconomic impact, the G7 countries need to align their interests and risk perceptions. At the same time, G7 members besides the United States should improve their ability to propose and enact geoeconomic measures. New and expanded G7 working groups should reflect the expansion of the G7's agenda to include financial stabilization, sanctions coordination, investment programs, trade restrictions, technology, and defense. In addition, G7 members must build institutional capabilities to share the administrative and policymaking burdens of geoeconomic measures more equally. Furthermore, the G7 should bolster its partnerships with like-minded countries by inviting them to participate in issue-specific working groups, investment initiatives, and political declarations.

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Introduction

Economic security ranked high on the agenda of the 2023 G7 cycle under the chairmanship of Japan. As stated in the G7 Hiroshima Leaders' Communiqué, the prime outcome document from the G7 Summit held in Hiroshima from May 19 to 21, 2023: "Ensuring economic resilience and economic security globally remains our best protection against the weaponization of economic vulnerabilities."[1] Accordingly, at this summit, the G7 committed to "enhance collaboration by launching the Coordination Platform on Economic Coercion to increase our collective assessment, preparedness, deterrence, and response to economic coercion."[2]

The G7 faces a new geopolitical and geoeconomic environment. Since February 24, 2022, Russia's invasion of Ukraine has sparked the worst conflict on the European continent since the end of the Second World War, initiating a turning point ("Zeitenwende") in international relations and the global economy. However, Russia's war against Ukraine is not the only driver of the new international environment. Rivalries between Western democracies and autocratic regimes, especially between the United States (plus increasingly the EU) and China, are intensifying. China has become a strategic rival and a systemic competitor for the West. Both developments are increasingly calling into question the mantra of "change through trade" that has guided the trade policies of Western democracies for decades.

In the light of these developments, the G7 has gained in importance. However, is the G7 a geoeconomic actor? A geoeconomic actor is characterized by the following traits: It has a distinct set of values and clearly defined economic and security interests.

- It has a vision or agenda for its own future as well as for the global economic and security order.
- It can quickly and effectively adopt strategies that reflect changes in the geopolitical and geoeconomic environment.
- It possesses a set of defensive and offensive instruments that can be readily employed to pursue said values, interests, and visions.
- It possesses the necessary political and economic weight to make these instruments meaningful.

In the face of Russia's war of aggression, the G7 members have shown great unity. The G7 is a community of shared values that stands for democracy, rule of law, respect for human rights, and the free market. Together, the 2020 election of US President Joe Biden and the recent sea change in German foreign policy represented by its "Zeitenwende" have allowed for stronger geoeconomic cooperation among the G7 countries. But how strong and sustainable is this new geoeconomic alignment – particularly in light of upcoming elections in the EU in June and the United States in November? Historically, the G7 countries have not always been of one mind when it comes to geopolitical and geoeconomic issues. The phase from 2016 to 2020, after Brexit and the election of Donald Trump as President of the United States, was especially taxing. Rifts emerged among the G7 countries on how to deal with the Covid-19 pandemic, trade and financial issues, as well as China, Iran, and Russia.

At the center of the following DGAP and Aspen Germany Analysis stands an assessment of the joint geoeconomic commitments and policies of the G7. Chapter 2 lays the groundwork by defining geoeconomics and what this means in the context of the G7. Chapter 3 presents three case studies – Russia, Iran, and China – that take a closer look at select geoeconomics instruments with a focus on trade. Each case study will begin with a brief description of the conflict between the G7 countries and that country. It will then give an overview of the applied sanctions and export controls followed by a summary of the degree of geoeconomic effectiveness of the G7 measures and alliance. Chapter 4 will sum up the findings of the case studies in terms of the central question: Is the G7 a geoeconomic actor? The study will close with recommendations to the G7.

1 G7, *Hiroshima Leaders' Communiqué*, May 20, 2023, p. 18: https://www.consilium.europa.eu/media/64497/g7-2023-hiroshima-leaders-communiqué.pdf (accessed January 4, 2024).

2 Ibid.

The Goals and Instruments of Geoeconomics and Geopolitics

The term "geoeconomics" describes many tools of statecraft, national security, and economic policy pursued by countries around the world. As such, the term has a variety of definitions that reflect its many applications. In their book *War by Other Means: Geoeconomics and Statecraft*, former US diplomats Robert Blackwill and Jennifer Harris describe geoeconomics this way: "The use of economic instruments to promote and defend national interests, and to produce beneficial geopolitical results."[3] Put more simply, Amano Tatsushi, Director General of the Strategic Research Department at the Japan Bank for International Cooperation, defines geoeconomics as "using the economy for geopolitical aims."[4] Although some see geoeconomics as a subset of geopolitics, others see the two as related but distinct terms. Whereas geoeconomic power projection is "more covert, conducted by economic means, and its operation logic is selective accommodation," geopolitical power projection is "an offensive foreign policy operation, is typically overt, conducted by military means, and its operational logic is confrontation."[5] This view places both geopolitics and geoeconomics within the larger category of "geostrategy," which can include a variety of military, economic, political, and other toolsets. In the following, geoeconomics is to be understood as strategies and policies that seek to advance national interests and shape the international landscape primarily through economic means.

The concept of combating adversaries through non-military means is not new. As Sun Tzu writes in *The Art of War*, "To subjugate the enemy's army without doing battle is the highest of excellence."[6] First coined in Edward Luttwak's 1990 article "From Geopolitics to Geo-Economics: Logic of Conflict, Grammar of Commerce," geoeconomics emerged in the post-Cold War period amid seismic changes in the economic and security landscape.[7] Following the collapse of the Soviet Union, the possibility of armed conflict between great powers receded, while American military hegemony disincentivized many nations from pursuing military options. After decades of arms races, nuclear standoffs, and proxy wars, when military power formed the basis for international influence, many hoped that nations would instead compete through economic means, a worldview encompassed by Francis Fukuyama's "End of History" paradigm. This shift was underpinned by the growth of globalized markets in the post-Bretton Woods economic order as well as efforts to insulate international economic policy from political considerations, including through the dispute resolution mechanisms of the World Trade Organization (WTO). Consequently, many nations' economic interests stretched around the globe via financial markets and supply chains. The projection of economic power assumed a more prominent role in national strategies, while military power projection became less relevant than during the Cold War. As these trends emerged, scholars embraced geoeconomics as a term that describes strategies to protect economic interests and project economic power globally.

In the past decade, the global landscape has shifted again; this time, toward what political economist Mark Blyth calls "neo-nationalism."[8] Whereas in the post-Cold War period major economic decisions such as signing trade and investment treaties focused on maximizing economic gains, today's policymakers frequently base economic relationships on security factors. This shift reflects the decline of post-World War II theories of peace: namely, that economic interdependence promotes peace by "increasing the value of trading over the alternative of aggression."[9] This theory factored

3 John F. Troxell, "Geoeconomics," *US Army University Military Review* 96, no. 1 (2018), p. 8: https://www.armyupress.army.mil/Journals/Military-Review/English-Edition-Archives/January-February-2018/Geoeconomicsfw (accessed December 1, 2023); Robert Blackwill and Jennifer Harris, *War by Other Means: Geoeconomics and Statecraft*, (Cambridge, 2016).

4 Amano Tatsushi, "Geopolitics is 'Realism.' Geoeconomics is its 'Economic Means.' Understanding the Complexity of the World," Japan Bank for International Cooperation, 2023: https://www.jbic.go.jp/en/information/today/today_202301/jtd_202301_sp1.html# (accessed December 9, 2023).

5 Mikael Wigell and Antto Vihma, "Geopolitics versus Geoeconomics: The Case of Russia's Geostrategy and its Effects on the EU," *Journal of the Royal Institute of International Affairs* 92, no. 3 (2016), p. 605: https://www.jstor.org/stable/24757627 (accessed December 9, 2023).

6 Ibid.

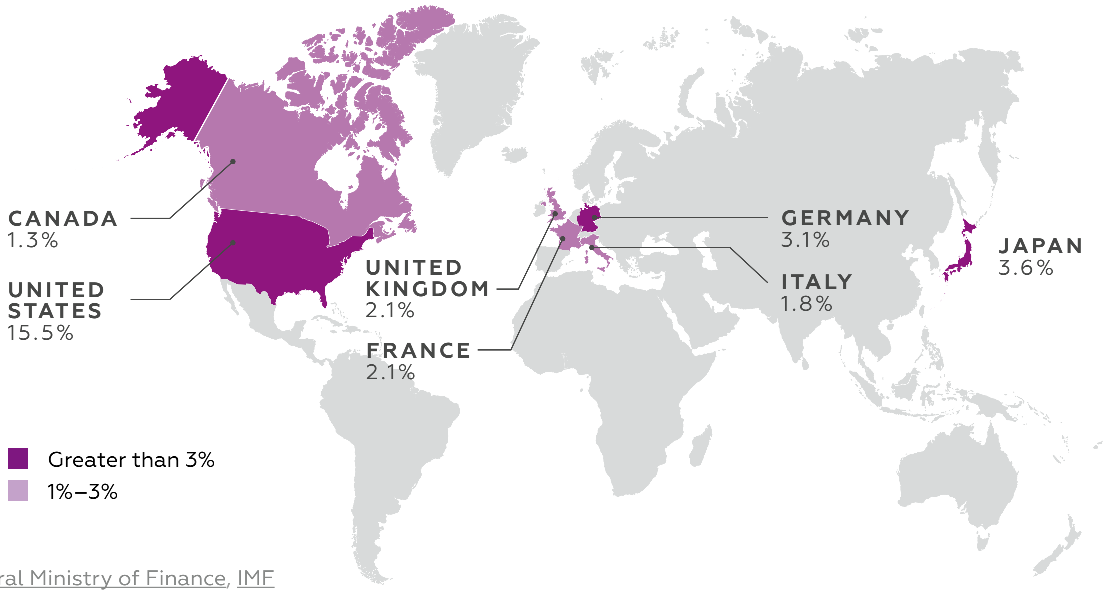
7 Edward Luttwak, "From Geopolitics to Geo-Economics: Logic of Conflict, Grammar of Commerce," *The National Interest*, no. 20 (1990), p. 17: https://www.jstor.org/stable/42894676 (accessed December 1, 2023).

8 Eric Lonergan and Corinne Sawers, *Supercharge Me: Net Zero Faster*, (Newcastle upon Tyne, 2022), p. 88.

9 Dale Copeland, "Economic Interdependence and War: A Theory of Trade Expectations," *International Security* 20, no. 4 (1996), p. 5: https://direct.mit.edu/isec/article-abstract/20/4/5/11525/Economic-Interdependence-and-War-A-Theory-of-Trade?redirectedFrom=fulltext (accessed December 9, 2023).

Share of Global GDP of Each G7 Country

As of April 15, 2024



Sources: Federal Ministry of Finance, IMF

security into economic relations more abstractly as a benefit of globalized markets in general, not specific trade or investment policies. Simultaneously, depending on trade to maintain the security landscape fostered the idea that maximizing economic gains in trade would not compromise security.

In the wake of Russia's full-scale invasion of Ukraine, policymakers now approach the relationship between trade and security much differently. Trade agreements still aim to have mutual economic benefits but are more often formulated with security imperatives in mind (for instance, the US-led Indo-Pacific Economic Framework for Prosperity (IPEF)). Since policymakers no longer see increasing trade as a path to an improved security environment, a relative convergence of economics and security can be observed.[10] Instead, many countries see economic relations as more of a zero-sum game and therefore act unilaterally to advance their economic interests. Some actions challenge the liberal international order, while others seek to maximize economic security within the bounds of international law. Rather than viewing trade as the prerequisite to peace, peace is more and more perceived as the prerequisite to trade.[11] This in turn reinforces the return of security as a prime factor in economic relations as well as the use of economic tools to improve military capabilities.

Geoeconomic approaches to trade, finance, aid, policy/standards setting, and information/cyber can encompass a variety of instruments – defensive and offensive. These geoeconomic tools can be categorized within four general areas: trade, finance, aid, and policy.[12] Some include information/cyber tools as a fifth category since these are frequently the product of national investments in digital or tech industries.[13]

An overview of these five categories can be found in the graphic at the top of the next page and here:

1. Geoeconomic tools in the area of trade include free trade agreements, subsidies for export-oriented industries, technology and production licensing, energy and commodities supply chains, trade defense instruments, and sanctions.
2. Financial instruments include regulations on the flow of capital, such as capital controls, currency manipulation, and sanctions on financial markets or firms. In addition, measures that utilize capital for specific goals – such as debt forgiveness, foreign direct investment (FDI), or investment in strategic domestic sectors – can be used for geoeconomic goals.
3. Geoeconomic foreign aid can promote infrastructure, bolster defense, develop state capacity, or address humanitarian crises.

10 Anthea Roberts et al., "Geoeconomics: The Variable Relationship Between Economics and Security," The Lawfare Institute, November 27, 2018: https://www.lawfaremedia.org/article/geoeconomics-variable-relationship-between-economics-and-security (accessed December 9, 2023).

11 Ibid.

12 Troxell, "Geoeconomics" (see note 3), p. 10.

13 Marianne Schneider-Petsinger, "Geoeconomics Explained," Chatham House, December 9, 2016: https://www.chathamhouse.org/2016/12/geoeconomics-explained (accessed December 1, 2023).

2 – G7 Geoeconomic Toolbox (Selected Instruments)

	DEFENSIVE*	OFFENSIVE**
TRADE	• Anti-dumping measures • Trade defense • Anticoercion instruments • Supply chain diversification • Anti-subsidy instruments • National security tariffs	• Trade sanctions • Export controls on dual-use goods • Resource partnerships • Export-oriented subsidies • Competition policy • Trade agreements (bilateral, plurilateral, multilateral) • Export credits and export credit insurance
FINANCE	• Capital controls • Investment screening • Investment protection agreements	• Investment partnerships • Financial market regulation • Financial sanctions • Investment facilitation agreements (bilateral, plurilateral, multilateral) • Investment insurance
AID		• Debt forgiveness • Financial or military assistance • Official development assistance
STANDARDS		• Domestic regulations, standards, and norms for emerging technologies and digitalization • International setting of standards and norms for emerging technologies and digitalization • Plurilateral and multilateral conventions on emerging technologies • Trade and technology agreements (bilateral, plurilateral, multilateral) • Bilateral and plurilateral mutual recognition agreements for regulations and standards
INFORMATION/ CYBER	• Countering industrial espionage • Cyber defense • Fighting digital manipulation • Disinformation countermeasures	• Cyber attacks • Cooperation agreements for cybersecurity • International specification for information security management system

*Defending against coercive or unfair foreign practices **Exerting influence abroad

Source: Authors' own compilation

4. Policy and standards setting in geoeconomics relies on regulatory sway to set standards and shape commercial activity, either in the domestic market or in foreign markets.[14]
5. Information and cyber tools can be considered part of the geoeconomic toolkit, particularly when a country's industries or technologies allow them to shape the information environment, steal valuable technologies, inflict economic damage through cyber tools, or alter foreign policies through election interference.[15]

In many cases, strategies can encompass multiple categories. For example, sanctions packages frequently combine trade and finance measures, while initiatives to secure critical supply chains rely on resource partnerships that involve trade, finance, aid, and regulatory measures. Typically, the specific instruments deployed by a nation reflect its comparative advantages, national interests, and ideology. As a result, geoeconomic conflicts can be multi-domain and asymmetric, combining political, economic, and military measures.

14 Troxell, "Geoeconomics" (see note 3), p. 10.

15 Schneider-Petsinger, "Geoeconomics Explained" (see note 13).

Three Case Studies

The following chapter presents three case studies: Russia, Iran, and China. Each of them begins with a brief description of the conflict between the G7 countries and the respective country, followed by an overview of the applied sanctions and export controls. A summary of the degree of geoeconomic effectiveness of the G7 measures and alliance closes each case study.

CASE STUDY 1: RUSSIA

What the Conflict Is About

After the formative phase of the G7 in the 1970s, it took two decades before another country was included in the group. Russia's inclusion resulted from strategic considerations to enhance cooperation in economic, energy and security matters during its transition phase after the end of the Cold War and to recognize its international stance after the collapse of the Soviet Union. This represented a departure from the group's values-based membership principle. In contrast, efforts to give China or other emerging economies such as India or Brazil an official seat at the table were denied, especially in the case of China due to a lack of shared values.

Russia was officially admitted in 1998, but it did not become a full member on fiscal and macroeconomic issues, the group's former core competence. G7 finance ministers and central bankers continued to meet in parallel with G8 leaders' summits.

After the Ukrainian Revolution of Dignity (Euromaidan) in February 2014, Russia annexed the Ukrainian peninsula of Crimea. On March 18, 2014, Russian President Vladimir Putin signed a treaty on the incorporation of Crimea into the Russian Federation. Russia also supported pro-Russian separatists in the Donbass region and created the case for separatism. For this purpose, the Wagner Group was founded. In response, the G7 issued a joint statement in the Hague on March 24, 2014, that condemned Russia's violation of Ukraine's territorial integrity and suspended Russia's G8 membership "until Russia changes course."[16] The expulsion was justified on the shared beliefs and responsibilities of the group. In 2014, Russia was also supposed to hold the rotating annual G8 presidency and was preparing the summit in Sochi. However, the remaining G7 countries canceled their participation in further G8 activities, de facto depriving Russia of its host status. The EU was then tasked with hosting an extraordinary G7 summit in Brussels in June 2014.[17]

In September 2014, the Trilateral Contact Group on Ukraine, consisting of Ukraine, Russia, and the Organization for Security and Co-operation in Europe (OSCE), negotiated the so-called Minsk Protocol with the aim to end the war in Donbass. After the failure of the first agreement, Minsk II was signed in February 2015 – during the German G7 presidency. Even though the fighting slowed down, a complete end was never achieved. The following years were characterized by a low intensity war in Eastern Ukraine.

In February 2022, Russia recognized the Donetsk People's Republic (DPR) and Luhansk People's Republic (LPR), deciding that the Minsk agreements were no longer valid. Finally, on February 24, 2022, Russia invaded Ukraine. The war continues at this writing.

G7 Declarations on Russia

In their Brussels Summit Declaration from June 2014 after the expulsion of Russia, the G7 state: "We confirm the decision by G7 countries to impose sanctions on individuals and entities who have actively supported or implemented the violation of Ukraine's sovereignty and territorial integrity and who are threatening the peace, security, and stability of Ukraine. (…) We stand ready to intensify targeted sanctions and to implement significant additional restrictive measures to impose further costs on Russia should events so require."[18]

In 2015, during the German presidency, the G7 stressed that the imposed sanctions should be linked "to Russia's complete implementation of the Minsk agreements and respect for Ukraine's sovereignty." The G7 stressed that the present sanctions and further

16 G7, *The Hague Declaration*, March 24, 2014, p. 2: https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/141855.pdf (accessed January 4, 2024).
17 G7, *G7 Brussels Summit Declaration*, June 5, 2014: http://www.g7.utoronto.ca/summit/2014brussels/declaration.html (accessed January 4, 2024).
18 Ibid.

restrictive measures could either be abandoned, once Russia fulfilled the agreements, or expanded, if demanded by Russia's actions.[19] This was a geoeconomic approach by the G7: the aim was to increase the (economic) costs on Russia if the political goal (to implement the Minsk agreement) was not fulfilled.

This line of thought was repeated in the Ise-Shima Declaration of the Japanese G7 Presidency in 2016, the Italian G7 Declaration from Taormina in 2017, and the G7 Communiqué from Charlevoix, Canada, in 2018. France took over in 2019, and its final G7 Leaders' Declaration, which is just one page long, states only that: "France and Germany will organize a Normandy format summit in the coming weeks to achieve tangible results."[20] In the wake of the pandemic, the US G7 summit in 2020 never took place.

In 2021, Russia started a large build-up of its military forces on Ukraine's borders, leading the G7 foreign ministers under the British presidency to issue a warning in December of that year: "Russia should be in no doubt that further military aggression against Ukraine would have massive consequences and severe cost in response." This was repeated on February 14, 2022, under the German Presidency: "Any further military aggression by Russia against Ukraine will be met with a swift, coordinated, and forceful response. We are prepared to collectively impose economic and financial sanctions which will have massive and immediate consequences on the Russian economy."[21]

After Russia's large-scale invasion of Ukraine on February 24, 2022, the G7 immediately condemned it as "a serious violation of international law and a grave breach of the United Nations Charter and all commitments Russia entered in the Helsinki Final Act and the Charter of Paris and its commitments in the Budapest Memorandum." And they promised to bring forward "severe and coordinated economic and financial sanctions."[22] The G7 summit in Elmau again reiterated the strong commitment of the G7 to use sanctions and other measures to react to Russia's war of aggression. "We are committed to sustaining and intensifying international economic and political pressure on President Putin's regime and its enablers in Belarus, depriving Russia of the economic means to persist in its war of aggression against Ukraine, and we will continue our targeted use of coordinated sanctions for as long as necessary, acting in unison at every stage. Our use of sanctions is in defence of the rules-based international order that Russia has so egregiously violated."[23]

In using this language, the G7 explicitly state their geoeconomic approach to use economic means to end the Russian war. At the latest Hiroshima summit in May 2023, the G7 leaders again supported this geoeconomic approach to coordinate sanctions and other economic actions to raise the costs of Russia's war and, by doing so, to undermine Russia's ability to continue its aggression. This approach includes three measures:

1. Further export controls on industrial machinery, tools, and other technology that Russia uses for its military actions;

2. The continued use of export bans and price caps for seaborne Russian crude oil and refined oil products, and further reductions on civil nuclear and related goods from Russia; and

3. The strengthening of financial sanctions by "preventing third-country branches of Russian banks from being used to avoid sanctions."[24]

Trade Instruments in Practice

In 2014, after the annexation of Crimea, individual G7 members started to impose sanctions against Russia. On the part of the EU, these included export and import restrictions. The EU also ended its talks on an EU-Russia agreement. However, the sanctions and export controls were so weak and the costs so low that they did not prevent (but rather encouraged, as some would argue) the increase of tensions and later the Russian invasion in February 2022.

19 G7, *Leaders Declaration G7 Summit*, June 7–8, 2015, p. 7: https://www.bundesregierung.de/resource/blob/998440/436680/e077d51d67486b1df34e539f621aff8c/2015-06-08-g7-abschluss-eng-en-data.pdf?download=1 (accessed January 4, 2024).

20 G7, *Elysée G7 Leaders' Declaration*, August 26, 2019: https://www.elysee.fr/en/g7/2019/08/26/g7-leaders-declaration (accessed January 4, 2024).

21 G7 Finance Ministers, *G7 Finance Ministers' Statement on Ukraine*, February 14, 2022: https://www.bundesregierung.de/resource/blob/998440/2021324/c8ccbe7cdb23eadcf5514955abb56c4f/2022-02-14-g7-finanzminister-en-data.pdf?download=1 (accessed January 4, 2024).

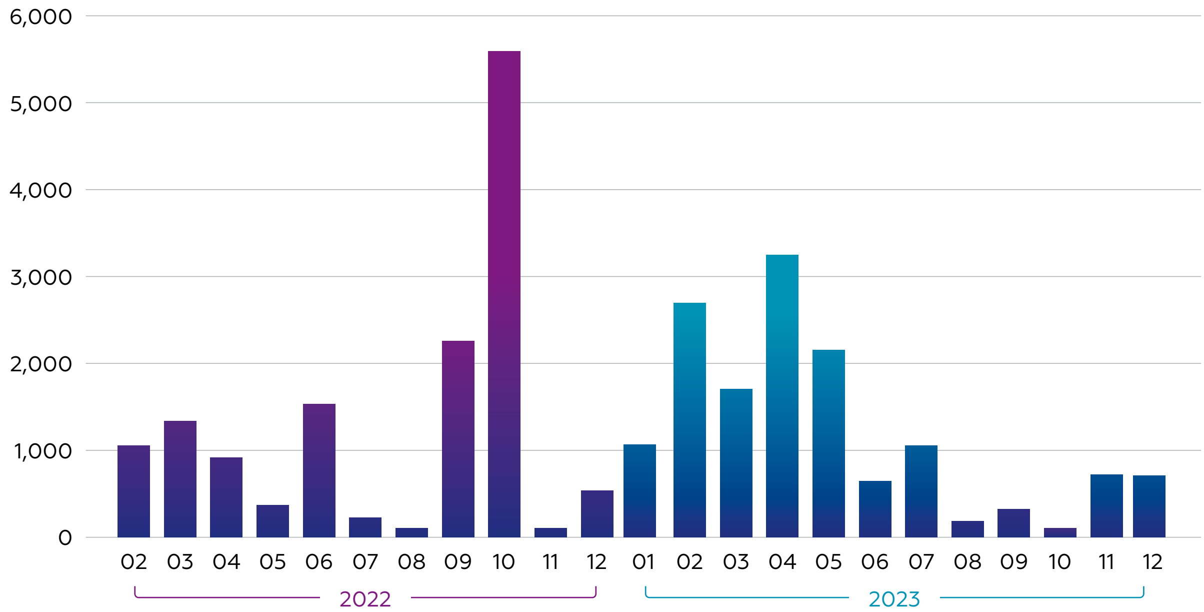
22 G7, *G7 Leaders' Statement on the Invasion of Ukraine by Armed Forces of the Russian Federation*, February 24, 2022, p. 1: https://www.g7germany.de/resource/blob/998352/2007730/6a4fc79947784765833b23ed762de76d/2022-02-24-g7-erklaerung-en-data.pdf?download=1 (accessed January 4, 2024).

23 G7, *G7 Statement on Support for Ukraine*, Elmau, June 27, 2022, p. 4: https://www.g7germany.de/resource/blob/974430/2057196/4628490eda0863e429c30136ec180feb/2022-06-27-g7-erklaerung-ukraine-en-data.pdf?download=1 (accessed January 4, 2024).

24 G7, *G7 Leaders' Statement on Ukraine*, Hiroshima, May 19, 2023, p. 4: https://www.g7hiroshima.go.jp/documents/pdf/230519-01_g7_en.pdf (accessed January 4, 2024).

3 – Russia Faces Thousands of Active Sanctions*

Number of Newly-Imposed Sanctions Against Russia
per Month since February 2022



*Sanctions that are still in effect as of January 9, 2024
Source: Statista

The G7 became much more forceful in their geoeconomic response after Russia's large-scale invasion of Ukraine in 2022. In March 2022, the G7 leaders pointed out that the G7 imposed "sweeping export bans and controls that cut Russia off from our advanced technologies."[25] Shortly afterward, the G7 leaders stressed their intention to isolate Russia economically and technologically by banning new investment in key sectors of the Russian economy, including the energy sector. The G7 also further extended trade export bans on advanced goods and specific services that are important to Russia's security, state, and economy.

In addition, the G7 decided to immediately increase import restrictions on a range of Russia's revenue-raising exports relating to state-owned entities, particularly in the defense sector. Furthermore, the G7 agreed to accelerate plans to reduce reliance on Russian energy (decoupling), including phasing out and banning Russian coal imports and reducing the dependency on Russian oil. In the Leaders' Communiqué from Elmau,[26] the G7 leaders reiterated their commitment to phase out or ban the import of Russian coal and oil. The G7 also intended to "further reduce reliance on civil nuclear and related goods from Russia."[27]

The G7 finally decided to prohibit all services that enable the transportation of Russian seaborne crude oil and petroleum products globally, unless the oil is purchased at or below a certain price cap. During the week of December 5, 2022, the price cap on seaborne Russian crude oil entered into force at $60 per barrel. In addition, the G7 agreed to introduce a price cap on Russian origin petroleum products starting in February 2023.[28]

25 G7, *G7 Leaders' Statement*, Bundesregierung, March 11, 2022, p. 1: https://www.bundesregierung.de/resource/blob/997532/2014234/39e142fa878dce9e420ef4d29c17969d/2022-03-11-g7-leader-eng-data.pdf?download=1 (accessed January 4, 2024).

26 G7, *G7 Leaders' Communiqué*, Elmau, June 28, 2022, p. 4: https://www.g7germany.de/resource/blob/974430/2062292/9c213e6b4b36ed1bd687e82480040399/2022-07-14-leaders-communique-data.pdf?download=1 (accessed January 4, 2024).

27 Ibid., p. 5.

28 G7 and Australia, *Statement of the G7 and Australia on a Price Cap for Seaborne Russian-origin Crude Oil*, December 2, 2022: https://www.auswaertiges-amt.de/en/newsroom/news/g7-australia-price-cap-seaborne-russian-origin-crude-oil/2567026 (accessed January 4, 2024).

In the G7 leaders' statement from February 24, 2023, which was issued one year after the Russian invasion, the G7 promise to "work collectively on further measures on Russian diamonds, including rough and polished ones."[29] In December 2023, the G7 finally agreed to impose a direct import ban on Russian diamonds starting in January 2024. This is connected to a new tracing system for diamonds.[30]

Finance Instruments in Practice

In 2014, the EU – in cooperation with other G7 members – also started to impose financial sanctions against Russia, including account closures. These financial instruments were further strengthened after the Russian invasion of Ukraine in 2022. In their statement from March 11, 2022, the G7 say: "We have collectively isolated key Russian banks from the global financial system (and) blunted the Central Bank of Russia's ability to utilise its foreign reserves."[31] In April 2022, the G7 declared that they had already significantly degraded Russia's financial system by targeting the transactions involving assets from the central bank and a number of other financial institutions.[32]

One month later, on May 8, 2022, the G7 stressed that – in addition to the Russian Central Bank and Russia's largest financial institutions – it continues to take action against Russian banks that are connected to the global economy and systemically critical to the Russian financial system. Finally, in their executive summary from Elmau on June 27, the G7 promises to further "reduce Russia's revenues, including from gold."[33] On May 19, 2023, the Hiroshima summit promised to further strengthen the financial sanctions by "preventing third-country branches of Russian banks from being used to avoid sanctions."[34]

Interim Conclusion

The G7's response after the Russian annexation of Crimea in 2014 was quite weak. One reason for this was the different interests and threat perceptions of the G7 members. The German government, for example, supported limited sanctions on representatives of the Russian elite. It was, however, more cautious regarding economic sanctions – not only out of fear of the economic repercussions for Germany but also as a warning against an escalation of the conflict with Russia. The more diplomatic approach that the German government pursued toward Russia was built on the country's "Ostpolitik," which dated back to the 1970s and was built on the idea of "change through rapprochement," and its "Neue Ostpolitik," which envisioned a "Partnership for Modernization." Thus, the German government followed the widespread belief that economic interdependence would reduce the risks of conflict (known as "Wandel durch Handel"; change through trade) and, consequently, saw it as important for stability in Europe.[35] Given economic interests and this mindset, which could even be called opportunism due to Germany's dependence on Russian gas,[36] it does not come as a surprise that the German government supported Nord Stream 2. This natural gas pipeline ran from Russia to Germany through the Baltic Sea and was financed by Gazprom and several European energy companies, including France's ENGIE, Germany's Uniper and Wintershall, Austria's OMV, and the Anglo-Dutch conglomerate Shell. France had also followed a diplomatic approach toward Russia, but it became much more critical of Nord Stream 2. In 2019/2020, the French government (also bargaining on the nuclear energy option) asked the German government outright to stop the controversial project.[37]

29 G7, *G7 Leaders' Statement*, February 24, 2023: https://ec.europa.eu/commission/presscorner/detail/en/statement_23_1229 (accessed January 4, 2024).

30 Laura Hülsemann and Barbara Moens, "G7 to Sanction Russian Diamonds as of January," *Politico*, December 6, 2023: https://www.politico.eu/article/g7-russia-diamonds-sanctions-ukraine-war-as-of-january (accessed January 4, 2024).

31 G7, *G7 Leaders' Statement*, Bundesregierung (see note 25).

32 G7, *G7 Leaders' Statement*, Berlin, April 7, 2022, p. 2: https://www.g7germany.de/resource/blob/997532/2024356/f5d27e428c7f4d0f4086bd6bbafc6da0/2022-04-07-g7-leaders-eng-data.pdf?download=1 (accessed January 4, 2024).

33 G7, *G7 Statement on Support for Ukraine*, Elmau (see note 26).

34 G7, *G7 Leaders' Statement on Ukraine*, Hiroshima (see note 24).

35 Konrad Popławski and Anna Kwiatkowska, "The German Reaction to the Russian-Ukrainian Conflict – Shock and Disbelief," Center for Eastern Studies, April 3, 2014: https://www.osw.waw.pl/en/publikacje/osw-commentary/2014-04-03/german-reaction-to-russian-ukrainian-conflict-shock-and (accessed December 1, 2023).

36 Stefan Meister and Wilfried Jilge, "After Ostpolitik: A New Russia and Eastern Europe Policy Based on Lessons from the Past," DGAP Analysis, April 28, 2023: https://dgap.org/en/research/publications/after-ostpolitik-0 (accessed March 7, 2024).

37 Albrecht Meier et al., "Streit um die Ostsee-Pipeline: Frankreich ist jetzt gegen Nord Stream 2" [Dispute over the Baltic Sea pipeline: France is now against Nord Stream 2], *Tagesspiegel*, February 7, 2019: https://www.tagesspiegel.de/politik/frankreich-ist-jetzt-gegen-nord-stream-2-5315884.html (accessed December 1, 2023).

The United States, on the other hand, was highly critical toward Russia and strongly opposed Nord Stream 2, warning against Russia's weaponization of its energy relations. During the Trump administration, several laws were passed by the US Congress targeting Russian pipeline projects and Western involvement. In 2017, the US Congress had passed the Countering Americas' Adversaries Through Sanctions Act (CAATSA), which included sanctions against Iran and North Korea as well as sanctions against individuals and companies that enhanced the ability of Russia to construct energy export pipelines or provide Russian goods or services that facilitate the expansion, construction, or modernization of energy export pipelines by Russia. In 2019, the US Congress had passed the Protecting Europe's Energy Security Act (PEESA), which encompassed sanctions against individuals and companies involved in the provision of ships for the laying of the Nord Stream 2 pipeline. In July 2020, the Protecting Europe's Energy Security Clarification Act (PESCAA) extended sanctions to individuals and companies.[38] The German-US rift over how to deal with Russia added to the conflictual nature of transatlantic relations during the Trump administration when several trade conflicts burdened the partnership. This put a damper on effective geoeconomic cooperation in the G7.

In contrast, the G7 response after Russia's large-scale invasion of Ukraine in 2022 was much more united and assertive. However, G7 countries succeeded neither in destroying Russia's war economy nor in changing Russia's determination to continue this invasion. Russian President Vladimir Putin did not abandon Russia's military aggression; instead, he warned the Russian population that they needed to prepare for a prolonged war.

Soon after the Russian invasion, the G7's economic and financial sanctions and export controls had a considerable impact: The value of Russia's currency, the rubel, decreased rapidly, forcing Russia to double its interest rates to fight capital flight.[39] In addition, Russian military-industrial production was heavily hit, forcing the country to import weapons and ammunition from Iran, North Korea, and (possibly) China. Therefore, in April 2022, the G7 Finance Ministers and Central Bank Governors summarized: "Our sanctions are already having the intended massive impact on the Russian economy, which is likely to contract significantly this year."[40]

Toward the end of 2022, however, it became apparent that Russia had managed the economic downfall better than expected. This changed in early December 2022 with the introduction of the oil price cap, which had a strong negative impact on Russian revenues. Russian exports weakened considerably and the rubel weakened as well. In July 2023, Russian Finance Minister Anton Siluanov announced that the hole in Russia's state budget would be bigger than previously expected. Due to the high expenditures for the war against Ukraine and reduced revenues from energy exports, the budget deficit could expand to 2.5 percent of GDP. However, the ministry stressed that Russia had sufficient resources to meet its planned expenditures.[41]

These positive effects of G7 sanctions lasted until the first half of 2023. Since then, Russian export earnings are back, leading to rising budget revenues for the country. In addition, Russia stabilized its macro-economy, experienced economic growth, enlarged its military production, and had a very low unemployment rate. There are several reasons for the limited impact of G7 sanctions (despite the existing oil price cap):

- The geopolitical uncertainties led to higher energy prices worldwide, which, in turn, led to higher oil revenues for Russia. In addition, price cap violations are increasing due to an expanding shadow fleet of vessels that transport Russian crude oil above the price cap through Baltic and Black Sea ports. The Kyiv School of Economics calculated that in October 2023, 99 percent of seaborne Russian crude oil was sold above the price cap using vessels of which more than 70 percent belonged to non-G7 countries.[42]

38 German Bundestag, "US-Sanktionen gegen den Bau der Pipeline Nord Stream 2 aus Völkerrechtlicher Sicht" [US sanctions against the construction of the Nord Stream 2 pipeline from an international law perspective], *Wissenschaftlicher Dienst*, 2021: https://www.bundestag.de/resource/blob/794744/5613bf9f65fa52fd7c1d06ec6f52ebb3/WD-2-075-20-pdf-data.pdf (accessed December 9, 2023); Robin Fehrenbach (ed.), "Die Sanktionsspirale der USA gegen Nord Stream 2" [The USA's spiral of sanctions against Nord Stream 2], *Atlantik Brücke Dossier*, 2020: https://www.atlantik-bruecke.org/die-sanktionsspirale-der-usa-gegen-nord-stream-2 (accessed January 4, 2024).

39 European Council, *Impact of Sanctions on the Russian Economy*, 2023: https://www.consilium.europa.eu/en/infographics/impact-sanctions-russian-economy (accessed January 22, 2023).

40 *G7 Finance Ministers' Statement* (see note 21).

41 "Russisches Staatsdefizit 2023 größer als erwartet" [Russian government deficit larger than expected in 2023], *Die Presse*, July 25, 2023: https://www.diepresse.com/13450690/russisches-staatsdefizit-2023-groesser-als-erwartet (accessed February 29, 2024).

42 Alan Beattie, "Why Export Controls are Failing to Cripple their Targets," *Financial Times*, December 7, 2023: https://www.ft.com/content/10f1f080-8eb3-44a0-b4c6-1106b457c915 (accessed December 1, 2023).

- Russia was prepared for the sanctions. Long before the war, the country had withdrawn its reserves from the US financial system and, looking for alternative trading partners, built stronger political and economic (trade) ties with China, India, and the Middle East.[43]

- Trade is also redirected to circumvent sanctions and export controls. In February 2023, just one year after Russia's large-scale invasion of Ukraine, the European Bank for Reconstruction and Development (EBRD) pointed to increasing trade flows to countries that neighbor Russia. From May to July 2022, exports from the EU, United States, and United Kingdom to Russia dropped by more than half (adjusted for inflation) compared to the average from 2017 to 2019. At the same time, however, sales from Europe and the United States to Armenia and Kyrgyzstan increased by more than 80 percent. Those two countries, in turn, more than doubled their exports to Russia during the same period, indicating a diversion of trade via new routes and, as such, a circumvention of sanctions.[44] In addition, while a report by a US-Ukrainian research team shows that export controls are a powerful instrument to curb Russian access to many products that are needed for military production – in particular advanced electronics – there is an enforcement problem. Supply chains have adapted, and Russia imports many products through third countries, including China.[45]

- The G7 sanctions, which omit the majority of consumer goods, are more limited in scope compared to US sanctions against Iran, North Korea, or Venezuela. Also, the United States did not impose secondary sanctions to prevent other countries from trading with Russia. In addition, several Russian banks are still linked to the international financial system.[46]

- To increase the effectiveness of export controls and sanctions, the G7 is dependent on the cooperation of the big emerging economies. Yet not all of them have explicitly condemned Russia's blatant violations of international law and human rights. In early March 2022, the UN General Assembly overwhelmingly adopted a resolution calling on Russia to immediately end its military operations in Ukraine. However, some G20 members abstained: China, India, and South Africa, among others. In mid-October 2022, the majority of UN members passed a resolution calling on countries not to recognize Russia's claim on the four occupied regions of Ukraine. China, India, and South Africa once again abstained. Most of the emerging economy countries of the G20 did not join the advanced market economy countries in imposing sanctions on Russia and do not comply with the price cap for oil.

Consequently, the G7 economic and financial sanctions and export controls against Russia were only partially effective for a brief time following the introduction of the oil price cap. With a growing lack of enforcement (shadow fleet), the sanctions are losing their credibility. The G7 are not big enough to truly prevent Russian oil sales to the Global South and other countries.

The medium- to long-term outlook for the Russian economy looks grim. Still, given ongoing military spending, one should not expect the Russian (war) economy to collapse any time soon – unless global oil and gas prices collapse first. And even though export controls on defense technology have severely hampered Russia's military capacity, many other middle-income countries are willing to step in.

So far, Russia has made no effort to end the war, proving that the economic and financial measures have failed in their political objective to achieve peace (if this was indeed the objective). Changes in strategy will likely come through a combination of economic warfare (sanctions and export controls with strengthened enforcement systems), military victories, and the delivery of modern weapons and ammunition to Ukraine. Thus, the military successes (hard power) of Ukraine will be one of the dominant factors in deciding the future of Russia's war. Economic sanctions need to be strengthened to play a supportive role in raising the domestic costs of this aggression.

43 Peter Harrell, "The Limits of Economic Warfare: What Sanctions on Russia Can and Cannot Achieve," *Foreign Affairs*, March 27, 2023: https://www.foreignaffairs.com/united-states/limits-economic-warfare (accessed April 1, 2023).

44 Sam Fleming and Daria Mosolova, "West Probes Potential Sanction Dodging as Exports to Russia's Neighbours Surge," *Financial Times*, February 23, 2023: https://www.ft.com/content/4961a96c-16ac-496b-8aba-16d6025e4dfe (accessed January 28, 2024).

45 Olena Bilousova et al, "Challenges for Export Controls Enforcement. How Russia Continues to Import Its Military Production," KSE Institute, 2024: https://kse.ua/wp-content/uploads/2024/01/Challenges-of-Export-Controls-Enforcement.pdf (accessed January 24, 2024).

46 Stefan Meister and David Jalilvand, "Sanktionen Gegen Russland: Fünf Lehren aus dem Fall Iran" [Sanctions against Russia: Five lessons from the Iran case], DGAP Policy Brief, June 2022: https://dgap.org/de/forschung/publikationen/sanktionen-gegen-russland (accessed March 7, 2024); Harrell, "The Limits of Economic Warfare" (see note 43).

CASE STUDY 2 IRAN

What the Conflict Is About

Conflicts between the Islamic Republic of Iran and members of the international community have persisted for nearly five decades and involved disputes across a range of issues. Relations between the United States and Iran have been tense since the 1979 Iranian Revolution and subsequent Iran Hostage Crisis. The 1983 bombing of US military barracks in Beirut worsened US-Iran relations, as did the accidental 1988 downing of an Iranian passenger airliner by a US Navy ship. In the 1990s, the United States began raising concerns about Iranian nuclear weapons research. Iran later supported militias that fought against the 2003 invasion of Iraq led by US troops.[47]

While the United States aggressively confronted Iranian activities in the 1980s and 1990s, the rest of the G7 held somewhat warmer relations with Iran. After the Iranian Revolution, European companies generally disengaged with the Iranian economy, but European governments did not sever ties.[48] In 2003, Japan's import of Iranian oil peaked at 16 percent of total Japanese crude oil imports.[49] At the same time, human rights have been a major concern: the Iranian crackdown on protests after the contested 2009 election was followed by the EU's first unilateral sanctions in 2010. Iran's actions against the Mahsa Amini protest movement resulted in additional EU sanctions in 2022.[50]

In 2006, US intelligence concluded that Iran was enriching uranium in pursuit of a covert nuclear arms program. As a result, much of the international community and the G7 supported the United States in a sanctions regime coordinated through the United Nations Security Council (UNSC).[51] After four rounds of UNSC sanctions from 2006 to 2010, Iran agreed to the Joint Comprehensive Plan of Action (JCPOA) with China, the EU, France, Germany, Russia, the United Kingdom, and the United States in 2015. Yet Iran's destabilizing activities in the Middle East, including its support for regional proxies and missile tests, continued. In response to these concerns and objections raised by Israel, the Trump administration withdrew the United States from the JCPOA in 2018 and reimposed sanctions.

In the 2020s, the relationship between the G7 and Iran has been dominated by proliferation and arms control issues, Iranian support for militia groups that have targeted US troops and commercial shipping throughout the region, and Iranian support for the Russian invasion of Ukraine. Recent flash points include the Russian use of Iranian-designed Shaheed drones; Iran's alleged support for the attacks on Israel on October 7, 2023; Iran's support for the Houthis' attacks on Red Sea shipping; and attacks by Iran and its proxies on US installations and personnel in Iraq, Jordan, and Syria.

G7 Declarations on Iran

In recent years, the G7 has focused on those actions by Iran that contribute to regional instability. G7 leaders have remained vocally committed to a peaceful settlement through the JCPOA, stating in the 2023 Hiroshima Vision for Nuclear Disarmament that "the Joint Comprehensive Plan of Action continues to provide a useful reference."[52] In April 2023, the G7 Non-Proliferation Directors Group reaffirmed its commitment to the maintenance of a "nuclear-weapon-free-zone" in the Middle East.[53] During Japan's G7 presidency in 2023, Japan advanced a diplomatic approach to return Iran to the JCPOA through nine official meetings, including a visit by Iranian Foreign Minister Hossein Amir-Abdollahian to Tokyo and a leaders' meeting on the sidelines of the UN General Assembly.[54] The Biden administration has revived talks for the United States to rejoin the JCPOA with the support of the EU, France, Germany, and the United Kingdom.

47 Council on Foreign Relations, *US Relations With Iran, 1953–2023*, 2023: https://www.cfr.org/timeline/us-relations-iran-1953-2023 (accessed January 5, 2024).

48 Hassan Ahmadian, "Iran – Mapping European Leverage in the MENA Region," European Council on Foreign Relations, 2019: https://ecfr.eu/special/mapping_eu_leverage_mena/iran (accessed January 5, 2024).

49 Garrett Nada and Alex Yacoubian, "Iran and Japan Struggle Over Ties and Trade," *The Iran Primer*, December 20, 2019: https://iranprimer.usip.org/blog/2019/dec/17/iran-and-japan-struggle-over-ties-and-trade (accessed January 5, 2024).

50 Council of the EU, *Iran: EU Adopts Additional Sanctions Against Perpetrators of Serious Human Rights Violations*, November 14, 2022: https://www.consilium.europa.eu/en/press/press-releases/2022/11/14/iran-eu-adopts-additional-sanctions-against-perpetrators-of-serious-human-rights-violations (accessed January 5, 2024).

51 Suzanne Maloney, "Sanctions and the Iranian Nuclear Deal: Silver Bullet or Blunt Object?", *Social Research* 82, no. 4 (2015), p. 890: https://www-jstor-org.revproxy.brown.edu/stable/44282146 (accessed January 5, 2024).

52 G7, *G7 Hiroshima Leaders' Communiqué*, p. 27 (see note 1).

53 G7, *Statement of the G7 Non-Proliferation Directors Group*, April 17, 2023: https://www.state.gov/statement-of-the-g7-non-proliferation-directors-group (accessed January 5, 2024).

54 Maziar Motamedi, "Iran's Foreign Minister in First High-level Visit to Japan since 2019," *Al Jazeera*, August 7, 2023: https://www.aljazeera.com/news/2023/8/7/irans-foreign-minister-in-first-high-level-visit-to-japan-since-2019 (accessed January 5, 2024).

Despite these developments, recent G7 statements highlighted other conflictual issues in the relationship with Iran. The G7 Leaders' Statement issued on December 6, 2023, called on Iran to "refrain from providing support for Hamas, Hezbollah, the Houthis, and other non-state groups, and to use its influence with those groups to de-escalate regional tensions."[55] The United States has cited the JCPOA's lack of action on ballistic missiles as evidence the agreement is incomprehensive and counterproductive. Recent Israeli governments have forcefully advocated this position, which may carry more weight with G7 members in the wake of attacks by Iran and Iranian-backed militias on civilian targets in Israel and the Red Sea. In addition, Iran's decision to supply unmanned aerial vehicles (UAVs) to Russia prompted condemnation from the G7 Non-Proliferation Directors Group in April 2023. The G7's agenda regarding Iran has broadened and cannot be fully separated into nuclear proliferation, arms sales, and human rights issues.[56] This attitude stands in contrast with the pre-2015 approach, which produced an agreement by successfully isolating the nuclear issue from Iran's other activities.

Trade Instruments in Practice

To counter Iran and change its behavior, G7 members have steadily isolated Iran from the global economy. Beginning in December 2006, four rounds of UNSC sanctions directed states to prevent the sale, supply, or transfer of "all items, materials, equipment, goods and technology which could contribute" to Iran's activities around enrichment and the delivery of weapon systems. Later rounds banned the provision of fuel or supplies to ships owned or contracted by Iran that were suspected of carrying prohibited cargo. UNSC sanctions resolutions underscored that sanctions were not to affect "legal economic activities," and targets were limited to specific sectors, entities, and individuals.[57]

The UNSC's relatively narrow sanctions regime was supplemented by broader measures implemented by the United States to target both US and foreign trade with Iran. Some of these sanctions predate the UNSC regime, such as restrictions under the Iran Sanctions Act of 1996 on investments, goods, and services that could maintain or expand Iran's oil industry.[58] Sanctions were significantly expanded by the Iran Freedom and Counter-Proliferation Act of 2012, which blocked access to US-based accounts and financial services for firms that provided "significant goods or services" – especially insurance – to the energy, shipping, or shipbuilding sectors in Iran.[59] Subsequent executive actions taken from 2012 to 2017 implemented a near-total embargo on commercial activity with Iran by banning the import or export of most goods, technology, and services by US persons or firms to Iran, including through third countries.[60] While the EU, Japan, and others adopted more targeted sanctions in accordance with UNSC resolutions, the threat of US secondary sanctions effectively cut Iran off from the global economy in all sectors outside of agricultural commodities, medicine, and other humanitarian goods.[61]

Although G7 members complied with US sanctions during the heyday of UNSC sanctions, significant differences emerged following the unilateral withdrawal of the United States from the JCPOA in May 2018. When the United States "snapped back" sanctions, the EU passed regulations extending its "blocking statute" to allow European companies to maintain commercial relationships with Iran and receive compensation for US penalties.[62] In addition, in 2019, nine EU member states and the United Kingdom established the Instrument in Support of Trade Exchanges (INSTEX) to facilitate trade in food, medicine, and medical supplies while shielding firms from US sanctions.[63] Despite initial plans to expand INSTEX to cover other types of trade, European government shareholders dissolved the entity in March 2023 amid increasing tensions with Iran.[64]

55 G7, *G7 Leaders' Statement*, December 6, 2023, p. 5: https://www.consilium.europa.eu/media/68615/g7-leaders-statement-2023-12-6.pdf (accessed January 5, 2024).

56 G7, *Statement of the G7 Non-Proliferation Directors Group* (see note 53).

57 Security Council Report, *UN Documents for Iran: Security Council Resolutions*: https://www.securitycouncilreport.org/un_documents_type/security-council-resolutions/?ctype=Iran&cbtype=iran (accessed January 5, 2024).

58 European Commission, *Commission Delegated Regulation (EU) 2018/1100*, 2018, pp. 3–4: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018R1100&from=EN (accessed January 22, 2024).

59 Office of Foreign Assets Control, *Guidance on the Sale of Food, Agricultural Commodities, Medicine, and Medical Devices by Non-US Persons to Iran*, 2013: https://ofac.treasury.gov/media/7846/download?inline; Swedish Club, Jack Reed LLP., *Iran: US Sanctions*, 2021: https://www.swedishclub.com/media_upload/files/Sanctions/US%20Sanctions%20Iran%20-%20September%202021.pdf (both accessed January 24, 2024).

60 Leslie Wroughton and Humeyra Pamuk, "US to End All Waivers on Imports of Iranian Oil, Crude Price Jumps," Reuters, April 22, 2019: https://www.reuters.com/article/idUSKCN1RX0QX; Code of Federal Regulations, *31 CFR Part 560 Subpart B – Prohibitions*, 2024: https://www.ecfr.gov/current/title-31/part-560/subpart-B (both accessed January 5, 2024).

61 Office of Foreign Assets Control, *Guidance on the Sale of Food* (see note 59).

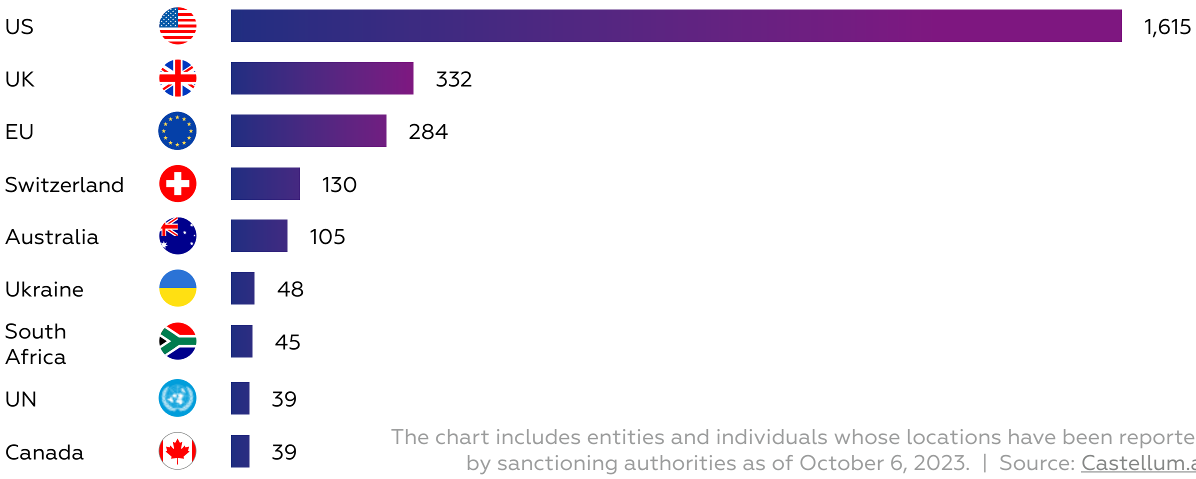
62 EU Iran Helpdesk, *The EU Blocking Statute*: https://sanctions-helpdesk.eu/blocking-statute (accessed January 5, 2024).

63 Europe Dissolves INSTEX Mechanism For Trade With Iran, *Iran International*, March 10, 2023: https://www.iranintl.com/en/202303104230 (accessed January 5, 2024).

64 Michael Lipin, "More European Nations Join Effort to Bypass US Sanctions on Iran," *Voice of America*, November 29, 2019: https://www.voanews.com/a/middle-east_voa-news-iran_more-european-nations-join-effort-bypass-us-sanctions-iran/6180238.html (accessed January 5, 2024).

4 – A Selection of Countries that Sanction Iran

Number of Their Designations of Iranian Entities and Individuals



The chart includes entities and individuals whose locations have been reported by sanctioning authorities as of October 6, 2023. | Source: Castellum.ai

After years of diverging sanctions policy during the Trump administration, the EU, United Kingdom, and United States coordinated new sanctions in July 2023 that target individuals and entities involved in Iran's UAV programs.[65] However, the G7 remains fractured. Even as alignment has increased on sanctions countering the Iranian arms trade, the EU and United States pursue diverging sanctions policies on the core issue of nuclear proliferation.

Finance Instruments in Practice

Financial sanctions were pursued by G7 members through the auspices of the UNSC. The three initial sanctions resolutions from 2006 to 2008 built a list of individuals and entities for asset freezes based on their support for Iran's "proliferation-sensitive nuclear activities." The resolutions also prohibited "financial assistance, investment, brokering, or other services" for listed individuals and entities seeking access to goods related to nuclear enrichment and ballistic missile programs. In 2010, the fourth round of UNSC sanctions authorized asset freezes for providers of financial services or insurance that contributed to Iran's nuclear weapons or ballistic missile programs and prohibited new partnerships between Iranian and foreign banks if they were suspected to relate to banned activities.[66]

The United States has enacted enforcement measures for many UNSC sanctions, taking advantage of the dependence of many traders and shippers on US financial firms. Since 2010, US banks have been prohibited from conducting transactions with foreign banks that have commercial activities with sanctioned Iranian entities.[67] Virtually all transactions with Iran's energy industry risk incurring sanctions under the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010, which extended economic sanctions from 1996 to 2016 and later 2026. In 2012, restrictions were expanded to the insurance industry under the Iran Threat Reduction and Syria Human Rights Act, which threatened to freeze the US-based accounts and financial services of insurance issuers in cases of noncompliance. After relaxing sanctions from 2015 to 2017, the United States reimposed unilateral sanctions after withdrawing from the JCPOA in 2018.[68]

Similarly to the United States, Japan and the EU have banned most transactions with Iran's energy sector since 2011. In 2012, the EU adopted similar measures to the United States, banning transactions with

65 Council of the EU, *Iran: EU Adopts New Restrictive Measures for Military Support to Syria and Russia's War of Aggression against Ukraine,* July 20, 2023: https://www.consilium.europa.eu/en/press/press-releases/2023/07/20/iran-eu-adopts-new-restrictive-measures-for-military-support-to-syria-and-russia-s-war-of-aggression-against-ukraine (accessed January 5, 2024).

66 Security Council Report, *UN Documents for Iran* (see note 57).

67 Clayton Thomas, "US Sanctions on Iran," Congressional Research Service, 2023: https://sgp.fas.org/crs/mideast/IF12452.pdf (accessed January 24, 2024).

68 Philip Heijmans, "US Sanctions Firms in Singapore, Malaysia Over Iran Petrol Links," Bloomberg, February 10, 2023: https://www.bloomberg.com/news/articles/2023-02-10/us-sanctions-firms-in-singapore-malaysia-over-iran-petrol-links (accessed January 21, 2024).

Iranian banks and cooperating with G7 members to freeze the Central Bank of Iran's assets and eject Iranian banks from the SWIFT electronic payment transfer system.[69] Japan also froze the assets of 15 Iranian banks and required authorization for transactions exceeding €40,000.[70] After the JCPOA was concluded in 2015, the EU, its member states, and Japan lifted most economy-wide financial sanctions on Iran, though some sanctions on entities related to nuclear or ballistic missiles have remained in place.[71]

Interim Conclusion

From 2006 to 2015, the G7 effectively coordinated sanctions and produced a diplomatic solution to the Iranian nuclear weapons program. Following the fourth round of UNSC sanctions and the expansion of US sanctions from 2010 to 2012, the Iranian economy contracted roughly 20 percent in the period from 2011 to 2015. The easing of sanctions following the JCPOA led to seven percent annual growth in the period from 2016 to 2018, but the "snap back" of US sanctions entailed an eight percent decline from 2019 to 2020. The primary cause of these swings appears to be Iran's crude oil exports, which declined from 2.5 million barrels per day (mbd) in 2011 to 1.1 mbd in 2014. Iranian industrial and automotive output also correlated to the imposition of sanctions, as did macroeconomic indicators such as inflation.[72] Iranian President Hassan Rouhani ran on a platform of redoubling negotiations in 2013 and subsequently agreed to freeze Iran's nuclear program in exchange for sanctions relief.

Since the withdrawal of the United States from the JCPOA in 2018, the G7 has ceased operating effectively as a sanctions-coordinating body. After the United States reimposed sanctions, the EU ramped up its blocking mechanism and the INSTEX trading platform to assist companies in avoiding US secondary sanctions. Japan resumed importing oil from Iran until 2019, when the Trump administration revoked its sanctions waiver.[73] Whereas the United States implemented a "maximum pressure" strategy, the EU sought to preserve relations with Iran and prove it could uphold the JCPOA on its own. However, Iran-EU trade crashed from €18.1 billion in 2018 to €5.1 billion in 2019. Similar figures were recorded in 2020 and 2021, reflecting the EU's failure to defy US sanctions and maintain the JCPOA.[74]

The expiration of UNSC sanctions in 2020 marked a key moment of disunity within the G7 and symbolized the United States' increasingly unilateral approach, as France, Germany, and the United Kingdom blocked a US attempt to extend the UNSC regime.[75] According to Iranian media, the expiration of the UNSC sanctions coincided with a significant increase in Iranian hydrocarbon export revenue from $19 billion in 2020 to $25 billion in 2021 and $42 billion in 2022 – though these figures could be a consequence of turbulence in energy markets following Russia's February 2022 invasion of Ukraine.[76]

The current difficulties in the G7's geoeconomic-measures against Iran stem from several issues:

- Fundamental disagreements over strategy have hampered consensus among G7 members. Under the Trump administration, the United States believed that "maximum pressure" would limit not only Iran's nuclear program, but also its malign activities in the region. Other JCPOA signatories and G7 members disagreed, arguing that a diplomatic agreement was the most reliable method to prevent Iran from developing a nuclear weapon. Whereas the United States regularly suffered missile and drone attacks from Iranian forces during this period, other G7 members did not face the same threats and therefore focused more narrowly on the nuclear dimension.

69 Kenneth Katzman, "Iran's Foreign and Defense Policies," Congressional Research Service, January 11, 2021: https://sgp.fas.org/crs/mideast/R44017.pdf(accessed January 24, 2024).

70 Michiyo Nakamoto, "Japanese bank freezes Iranian assets," *Financial Times*, May 17, 2012: https://www.ft.com/content/4c20d056-a00c-11e1-90f3-00144feabdc0 (accessed January 21, 2024).

71 Thomas, "US Sanctions on Iran" (see note 67).

72 Ibid.

73 Bernd Riegert, "How the EU Plans to Get Around US Sanctions on Iran," *Deutsche Welle*, July 8, 2018: https://www.dw.com/en/how-the-eu-plans-to-get-around-us-sanctions-on-iran/a-44981319 (accessed January 5, 2024); Nada and Yacoubian, *Iran and Japan Struggle Over Ties and Trade* (see note 49).

74 Beatrix Immenkamp and Julie Claustre, "EU Relations with Iran," European Parliamentary Research Service, 2023: https://www.europarl.europa.eu/RegData/etudes/BRIE/2023/739317/EPRS_BRI(2023)739317_EN.pdf; David Ramin Jalilvand, "EU-Iran Relations: Iranian Perceptions and European Policy," *PODEM*, 2019: http://podem.org.tr/en/researches/eu-iran-relations-iranian-perceptions-and-european-policy (both accessed January 5, 2024).

75 Security Council Report, *UN Documents for Iran* (see note 57); Nike Ching, "US 'Snaps Back' UN Sanctions on Iran," *Voice of America*, September 19, 2020: https://www.voanews.com/a/usa_us-snaps-back-un-sanctions-iran/6196117.html (accessed January 21, 2024).

76 Ali Ahmadi, "Is Biden Ignoring Iran's Sanctions Evasion?", *Foreign Policy*, December 5, 2023: https://foreignpolicy.com/2023/12/05/biden-iran-sanctions-evasion-oil-exports-enforcemen (accessed January 21, 2024).

- G7 members have vastly different capacities for crafting and enforcing sanctions policies. The United States has had extensive experience with financial sanctions since the administration of President George W. Bush extended due diligence and reporting mechanisms to prevent the financing of terrorist groups.[77] Many US statutes enacted to combat terrorism subsequently targeted Iran: for instance, the designation of the Central Bank of Iran as a terrorist entity in 2019, which eliminated access to its foreign exchange accounts.[78] By contrast, the EU's competency for sanctions enforcement lies with its member states, which did not adopt a uniform standard for the penalties faced for sanctions evasion until 2022.[79] The G7 has some competency through the Financial Action Task Force (FATF), which combats terrorist financing and has blacklisted Iran for over a decade.[80] However, the ability of the United States to quickly develop sanctions and enforce them via US-based financial firms has fostered a dependence on US sanctions policies that are coordinated – but not developed – through the G7.

- Tensions between the G7 and other major economies have undermined the effectiveness of sanctions. UNSC sanctions had broad acceptance, including from China and Russia. Today, Chinese demand for Iranian oil and the signing of the China-Iran economic pact in 2021 has helped to double Iranian energy export revenues between 2021 and 2022.[81] Rising global demand for affordable energy, particularly in the Global South, has created opportunities for black market vessels to deliver Iranian oil in defiance of sanctions, as has the sharing of counter-sanctions strategies among Iran, China, and Russia.[82] The growth of markets that are insensitive to G7 sanctions has allowed Iran to grow without sanctions relief, undermining the basic premise of the G7's sanctions strategy.

- Weak sanctions enforcement has created opportunities for Iran to "sanctions-proof" its economy. Iranian Supreme Leader Ali Khamenei has championed a "resistance economy" that embraces import substitutions as a path to self-sufficiency. Hardliner Ibrahim Raisi won the 2021 Iranian presidential election and has boosted ties with China and Russia. With Russia now facing a similar sanctions regime to Iran, and China preparing for a Taiwan Strait scenario, the three countries may be learning from each other's experiences, thereby dulling the effect of sanctions.[83]

Nearly ten years after the JCPOA, the G7 has no unified sanctions policy toward Iran, and its ability to shape Iranian behavior is greatly diminished. Recent developments – especially Iran-backed Houthi attacks in the Red Sea and Iran's support for Russia in Ukraine – may move the threat perceptions of the EU and its member states toward the position of the United States, therefore improving G7 unity.[84] However, in the absence of a plausible path to a negotiated settlement, Iran has tried to use military escalations to force the United States back to the negotiating table or to withdraw its forces from the region.[85] Multiple factors push the G7 and its members to respond with military force: the precedent established through airstrikes on the Houthis, the G7 issuing direct warnings against Iran in December 2023, and Iran's continued supply of drones to Russia's invasion of Ukraine. Iran has already survived a "maximum pressure" sanctions strategy and now finds common cause with Russia in circumventing sanctions regimes; it seems unlikely that sanctions alone could significantly alter Iranian calculations.

77 Maloney, "Sanctions and the Iranian Nuclear Deal," p. 892 (see note 51).

78 Thomas, "US Sanctions on Iran" (see note 67).

79 European Commission, *Proposal for a Council Decision 2022/0176*, 2022, pp.1–2: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM%3A2022%3A0247%3AFIN (accessed January 5, 2024).

80 Financial Action Task Force on Money Laundering, *Iran*, February 23, 2024: https://www.fatf-gafi.org/content/fatf-gafi/en/countries/detail/iran.html (accessed February 25, 2024).

81 Ahmadi,"Is Biden Ignoring Iran's Sanctions Evasion?" (see note 76).

82 Heijmans, "US Sanctions Firms in Singapore, Malaysia" (see note 68); Tom Keatinge, "Developing Bad Habits: What Russia Might Learn from Iran's Sanctions Evasion," Royal United Services Institute, June 6, 2023: https://www.rusi.org/explore-our-research/publications/occasional-papers/developing-bad-habits-what-russia-might-learn-irans-sanctions-evasion (accessed January 21, 2024).

83 Keatinge, "Developing Bad Habits" (see note 82).

84 David Lynch and Evan Halper, "Houthi Attacks are Starting to Reshape Shipping Flows," *The Washington Post*, January 17, 2024: https://www.washingtonpost.com/business/2024/01/16/shipping-houthi-attack-energy-prices/#:~:text=Since%20the%20outbreak%20of%20fighting,around%20%2415%2C000%20two%20years%20ago (accessed January 28, 2024).

85 Thomas, "US Sanctions on Iran" (see note 67); Mohammed Ayoob, "What Will Happen to the Nuclear Deal under Iran's New President?", *The Strategist*, June 25, 2021: https://www.aspistrategist.org.au/what-will-happen-to-the-nuclear-deal-under-irans-new-president (accessed January 21, 2024).

CASE STUDY 3 CHINA

What the Conflict Is About

Many issues plague the relationship between the People's Republic of China ("PRC" or "China") and members of the G7. These range from territorial disputes and human rights issues to economic coercion and disagreements regarding global governance. G7 members object to China's authoritarian government and illiberal economic system, which have presented barriers to achieving stable diplomatic and commercial ties. Human rights in China are frequently a topic of concern, especially after events that have highlighted or heightened internal repression such as the occupation of Tibet in 1952, the Tiananmen Square Massacre in 1989, the mass internment and alleged genocide of ethnic Uyghurs since 2014, and the repression of Hong Kong's democracy that culminated in 2020. For its part, Chinese historical memory of Japanese war crimes during the Second Sino-Japanese War and World War II remains relevant and provides a justification for its allegations of Western hypocrisy on human rights issues.

In territorial disputes with India and Taiwan, as well as in the South and East China Seas, the G7 opposes the Chinese position. Japan has active disputes with China over the Senkaku Islands – known in China as the Diaoyu Islands – and the United States and Japan supported the Philippines' landmark case against China under the UN Convention on Law of the Sea (UNCLOS). China has viewed these actions as interference in internal matters and an attempt to contain it.

Though the economic relationship between China and G7 members flourished in the 1990s and 2000s, since 2013, the Xi Jinping presidency has stoked Chinese nationalism and used Chinese geoeconomic power for coercive and destabilizing purposes. In 2010, China abruptly restricted the export of rare earth elements to Japan, using its dominance in critical minerals markets to punish Japan after a diplomatic dispute. The Chinese Belt and Road Initiative (BRI) has provided alternatives to G7 development programs. G7 nations are increasingly threatened by China's illiberal economic activities: industrial espionage, forced technology transfer, currency manipulation, and the deliberate distortion of global markets. This is viewed as a pattern of aggressive Chinese behavior involving economic coercion, interference in democratic elections, rapid military modernization, and technological and material support for Russia's military industry to enable attacks on Ukraine.

G7 Declarations on China

In recent years, the G7 has regarded China as a competitor and, in some areas, a systemic rival. The 2022 G7 Leaders' Communiqué urged China "to abstain from threats, coercion, intimidation, or the use of force" and commit to a "free and open Indo Pacific, which is inclusive and based on the rule of law."[86] The statement called attention to Chinese behavior in Xinjiang, Tibet, Hong Kong, the Taiwan Strait, and the East and South China Seas, emphasizing the broad scope of issues in the relationship between China and the G7. In 2023, these concerns were expanded in the G7 Leaders' Communiqué from Hiroshima, which devoted substantially more attention to China than any other geopolitical issue save Russia's war on Ukraine. Economic coercion stands out as a major focus of the Communiqué, which announces a Coordination Platform on Economic Coercion to "increase our collective assessment, preparedness, deterrence and response to economic coercion… [and] to protect global supply chains from illegitimate influence, espionage, illicit knowledge leakage, and sabotage in the digital sphere."[87] The weight given to economic security reflects Japan's interest in countering Chinese coercion following the 2010 China-Japan rare earths dispute.[88] Although both documents stress areas for cooperation with the PRC, the tone and focus on countering Chinese coercion points to a stronger consensus and shared urgency among G7 members regarding the threats posed by China.

Trade Instruments in Practice

Among the various geoeconomic tools employed by G7 members against China, an arms embargo is perhaps the longest standing. Established in 1989 following the Tiananmen Square Massacre, the US and EU embargoes have been carried out to differing extents by all G7 members. The United States has instituted a legally binding export ban of lethal and nonlethal military equipment, as well as equipment that could be

86 G7, *G7 Leaders' Communiqué*, Elmau, p. 17 (see note 26).

87 G7, *Hiroshima Leaders' Communiqué*, p. 18 (see note 1).

88 Jun Osawa, "How Japan Defines Economic Security," Wilson Center, March 6, 2023: https://www.wilsoncenter.org/publication/how-japan-defines-economic-security (accessed December 1, 2023).

used for domestic repression. The United States has also restricted the export of dual-use items and the reexport of foreign-produced components made with US technology or machinery by designating "entities of concern" that could facilitate illicit transfers to the Chinese military.[89] Unlike the legally enforceable US embargo, the EU embargo is a political declaration subject to interpretation and implementation by its member states, which have allowed extensive exports of nonlethal equipment and dual-use components directly to the Chinese military.[90] In addition, coproduction agreements between European and Chinese defense companies have transferred sensitive technical expertise to China.[91]

Since 2017, G7 members led by the United States have pursued new restrictive trade policies – first against Chinese telecom firms and later the Chinese semiconductor industry. From 2017 to 2019, the US Congress and Federal Acquisitions Regulations Council prohibited defense programs, federal agencies, and federal contractors from using Huawei equipment or services.[92] These measures evolved into a "rip and replace" program funded by the Federal Communications Commission (FCC) that banned new equipment sales and worked to phase out Huawei and ZTE's presence in rural wireless networks in the United States, an area where the two companies held a market share of approximately 25 percent.[93]

What began as a domestic public procurement ban in 2017 has expanded into efforts to cripple Chinese telecom and electronics firms by denying access to crucial inputs produced or designed by US entities. These measures extended globally through the Foreign Direct Product Rule (FDPR), which prevents the sale to Chinese telecom firms of restricted items produced using US technology, software, or machinery – regardless of their place of manufacture.[94] In October 2022, the United States broadened its focus, requiring an export license to ship "advanced computing integrated circuits… and certain semiconductor manufacturing items" to organizations on the Entity List, which was expanded to include many Chinese firms, research institutes, and government organizations. The United States also restricted the activities of US persons working on sensitive technologies for Chinese firms.[95] These efforts respond to growing concerns, especially from the United States and Japan, about Chinese civil-military fusion and the inability of G7 members to guarantee that their exports did not support the modernization of China's military.[96]

After instituting a domestic sanctions regime, the United States increased diplomatic outreach to convince allies of the security risks of Chinese telecom equipment. Subsequently, Canada, Japan, and the United Kingdom have banned Huawei and ZTE and set firm phase-out dates before 2030.[97] Since 2020, the European Commission has banned Huawei and ZTE from its own telecom procurement and issued a 5G Cybersecurity Toolbox that includes a framework for EU member states to issue restrictions on "high-risk suppliers." However, in June 2023, EU Internal Market Commissioner Thierry Breton called on member states to cease "lagging behind" in the effort to restrict

89 Oliver Bräuner et al., "Western Arms Exports to China," Stockholm International Peace Research Institute Policy Paper 43 (2015), p. 10: https://www.sipri.org/sites/default/files/files/PP/SIPRIPP43.pdf (accessed January 19, 2024).

90 Dan Sabbagh, "UK Sells Arms to Nearly 80% of Countries under Restrictions, Says Report," *The Guardian*, January 26, 2021: https://www.theguardian.com/world/2021/jan/26/uk-sells-arms-to-nearly-80-of-countries-under-restrictions-shows-report (accessed January 24, 2024).

91 Amanda Rivkin, "German Technology Found in China's Warships: Report," *Deutsche Welle*, June 11, 2021: https://www.dw.com/en/german-engine-technology-found-in-chinese-warships-report/a-59740301 (accessed January 24, 2024).

92 Jill Gallagher, "US Restrictions on Huawei Technologies: National Security, Foreign Policy, and Economic Interests," Congressional Research Service, January 5, 2022: https://crsreports.congress.gov/product/pdf/R/R47012/2#page9 (accessed January 28, 2024).

93 Cecilia Kang, "'Rip and Replace': The Tech Cold War Is Upending Wireless Carriers," *The New York Times*, May 9, 2023: https://www.nytimes.com/2023/05/09/technology/cellular-china-us-zte-huawei.html?smid=nytcore-ios-share&referringSource=articleShare; William Yuen Yee, "With US Restrictions on Huawei and ZTE, Where Will Rural America Turn?", Center for Strategic and International Studies, December 10, 2020: https://www.csis.org/blogs/new-perspectives-asia/us-restrictions-huawei-and-zte-where-will-rural-america-turn (both accessed January 19, 2024).

94 Mathieu Pollet and John Hendel, "The West is on a World Tour Against Huawei," *Politico*, November 28, 2023: https://www.politico.eu/article/west-world-tour-huawei-china-telecom (accessed January 28, 2024); Crowell, "BIS Publishes Final 'Direct Product' Rule for Huawei and Entity List Compliance Obligation Clarifications," August 21, 2020: https://www.crowell.com/en/insights/client-alerts/bis-publishes-final-direct-product-rule-for-huawei-and-entity-list-compliance-obligation-clarifications (accessed January 24, 2024).

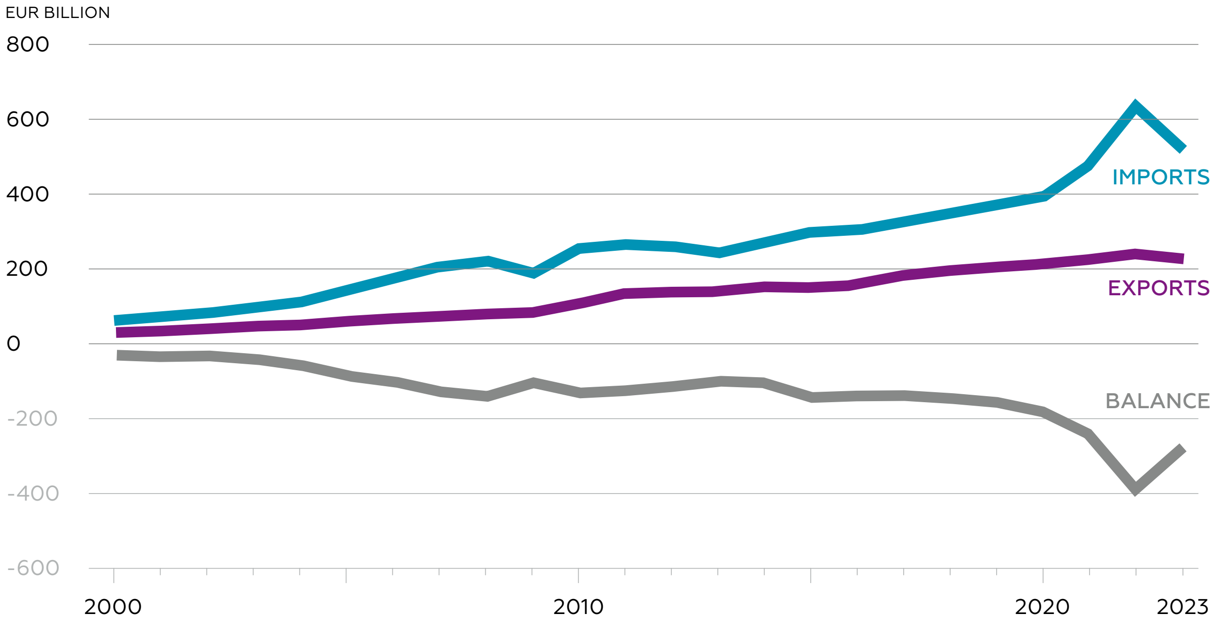
95 US Department of Commerce, *Implementation of Additional Export Controls: Certain Advanced Computing and Semiconductor Manufacturing Items; Supercomputer and Semiconductor End Use; Entity List Modification*, October 13, 2022: https://www.federalregister.gov/documents/2022/10/13/2022-21658/implementation-of-additional-export-controls-certain-advanced-computing-and-semiconductor (accessed January 19, 2024).

96 Elvire Fabry et al., "Shields Up: How China, Europe, Japan and the United States Shape the World through Economic Security," Jacques Delors Institute, February 2024, p. 17: https://institutdelors.eu/wp-content/uploads/2024/02/PP298_Comparing-_Economic_Security_Strategies_Fabry_Kohler-Suzuk_Lamy_Sibona_EN.pdf (accessed March 12, 2024).

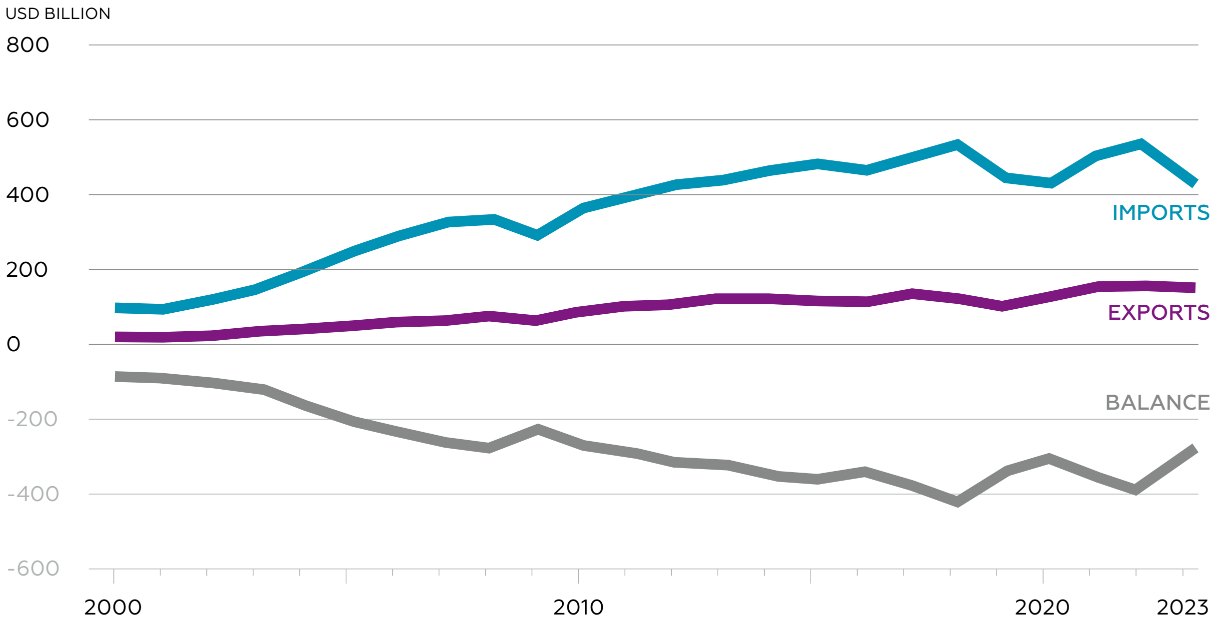
97 Government of Canada, Policy Statement – Securing Canada's Telecommunications System, May 2022: https://www.canada.ca/en/innovation-science-economic-development/news/2022/05/policy-statement--securing-canadas-telecommunications-system.html; "Japan Sets Policy that Will Block Huawei and ZTE from Public Procurement as of April," *The Japan Times*, December 10, 2018: https://www.japantimes.co.jp/news/2018/12/10/business/japan-sets-policy-will-block-huawei-zte-public-procurement-april/#.XImX-RNKj6A; Paul Sandle, "UK Extends Deadline to Remove Huawei Equipment from 5G Network Core," Reuters, October 13, 2022: https://www.reuters.com/business/media-telecom/uk-extends-deadline-remove-huawei-equipment-5g-network-core-2022-10-13 (all accessed January 19, 2024).

5 – Trade in Goods with China

EU-Trade in Goods with China
2000–2023



US-Trade in Goods with China
2000–2023



Source: Authors' own compilation based on eurostat and US Census Bureau

Huawei and ZTE due to high costs.[98] Germany's Deutsche Telekom is proceeding with its 2019 partnership that called Huawei a "strategic partner" and "key for our 5G plans."[99] France ceased renewing some Huawei equipment licenses in 2020 but has extended others and appeared to greenlight Huawei's first European factory in December 2023.[100]

Finance Instruments in Practice

Whereas trade sanctions and export controls have generally been led by the United States, multiple G7 members have developed geoeconomic initiatives involving financial instruments.

To address human rights violations, G7 members have issued coordinated sanctions against Chinese officials and entities. In 2021, Canada, the EU, the United Kingdom, and the United States responded to Chinese repression of ethnic Uyghurs by imposing asset freezes and travel bans on a small group of Chinese officials and the Xinjiang Production and Construction Corp.[101] Since 2020, G7 members have complied with the United States' Hong Kong Autonomy Act, which froze the assets of individuals who "attempt to materially contribute to the failure of the Government of China to meet its obligations under the Joint Declaration or the Basic Law." The law also issued secondary sanctions against foreign financial institutions that did business with sanctioned individuals.[102] The EU has vocally supported these efforts, including through a European Parliament resolution, but has not adopted its own measures.[103]

Investment screening, both inbound from and outbound to China, has become more popular with some G7 members. The United States is again a leader in this area; its Committee on Foreign Investment in the United States (CFIUS) has reviewed inbound foreign investments since 1975.[104] Prior to issuing trade sanctions for Chinese telecom firms, the United States blocked Huawei and ZTE's efforts to obtain US technology through investments or the acquisition of US firms.[105] Since 2020, the EU's FDI Screening Regulation has required member states to consult with the Commission when foreign investment could "risk affecting security or public order in more than one Member State or have an impact on strategic projects or programs of interest to the whole EU."[106] These rules stem from concerns regarding technology transfer to China after its acquisition of European companies. Current proposals from the Commission on economic security would represent a "doctrinal shift" by strengthening and centralizing screening for sensitive industries – though many member states remain hesitant to restrict commercial ties with China.[107] The Canadian Senate is debating new inbound investment rules, partially in response to US criticism of a Chinese telecom company's acquisition of a Canadian satellite technology firm.[108] Japan expanded its inbound investment screening regime to cover nine sensitive industries in May 2023.[109]

Regarding outbound investment, the United States has required investments in sensitive Chinese industries such as semiconductors, quantum information technology, and AI to receive approval since

98 Ryan Browne, "EU Urges More Countries to Ban China's Huawei, ZTE From 5G Networks," CNBC, June 16, 2023: https://www.cnbc.com/2023/06/16/eu-urges-more-countries-to-ban-chinas-huawei-zte-from-5g-networks.html (accessed January 19, 2024).

99 Laurens Cerelus, "How US Restrictions Drove Deutsche Telekom and Huawei Closer Together," *Politico*, July 6, 2020: https://www.politico.eu/article/deutsche-telekom-huawei-us-security-measures (accessed January 19, 2024).

100 Tristan Veyet et al., "European Countries Who Put Curbs on Huawei 5G Equipment," Reuters, September 29, 2023: https://www.reuters.com/technology/european-countries-who-put-curbs-huawei-5g-equipment-2023-09-28 (accessed January 24, 2024); Supantha Mukherjee, "Huawei to Start Building First European Factory in France Next Year – Source," Reuters, December 11, 2023: https://www.reuters.com/technology/huawei-start-building-first-european-factory-france-next-year-source-2023-12-11 (accessed January 19, 2024).

101 Foreign, Commonwealth & Development Office, *UK Sanctions Perpetrators of Gross Human Rights Violations in Xinjiang, Alongside EU, Canada and US*, 2021: https://www.gov.uk/government/news/uk-sanctions-perpetrators-of-gross-human-rights-violations-in-xinjiang-alongside-eu-canada-and-us (accessed January 19, 2024).

102 Office of Foreign Assets Control, *Hong Kong-related Sanctions*, 2020: https://ofac.treasury.gov/faqs/topic/5571 (accessed 19 January 2024).

103 Finbarr Bermingham, "Alarmingly Deteriorating' Situation: EU Lawmakers Renew Calls for Sanctions on Hong Kong Leaders," *South China Morning Post*, June 15, 2023: https://www.scmp.com/news/china/diplomacy/article/3224229/alarmingly-deteriorating-situation-eu-lawmakers-renew-calls-sanctions-hong-kong-leaders (accessed January 19, 2024).

104 Harry Broadman, "As CFIUS Turns 45 Years Old, US Regulation of Foreign Investment Is The Strictest Among Advanced Countries," *Forbes*, November 30, 2019: https://www.forbes.com/sites/harrybroadman/2019/11/30/as-cfius-turns-45-years-old-us-regulation-of-foreign-investment-is-the-strictest-among-advanced-countries (accessed January 19, 2024).

105 Gallagher, "US Restrictions on Huawei Technologies" (see note 92).

106 European Commission, *Updated Data on EU FDI Screening and Export Controls*, October 19, 2023: https://ec.europa.eu/commission/presscorner/detail/en/ip_23_5125 (accessed January 19, 2024).

107 Andy Bounds, "EU Scales Back China Investment Screening Plans to Avoid 'Turf War,'" *Financial Times*, January 24, 2024: https://www.ft.com/content/5baeab2d-6ef6-4882-80b7-9c2e4e186f35 (accessed January 28, 2024); Elvire Fabry et al., "Shields Up," p. 19 (see note 96).

108 Nicolas Pellicer-Garcia et al., "Canada Should 'De-risk' from China by Updating its Foreign-Investment Screening," Institute for Research on Public Policy, *Policy Options*, 2023: https://policyoptions.irpp.org/magazines/december-2023/canada-china-de-risk (accessed December 18, 2023).

109 United Nations Conference on Trade and Development, "Japan Adds Nine Sectors to the FDI screening Regime," April 24, 2023: https://investmentpolicy.unctad.org/investment-policy-monitor/measures/4294/adds-nine-sectors-to-the-fdi-screening-regime (accessed January 28, 2024).

August 2023.[110] Other G7 members, including the EU, are considering similar measures but are still in the deliberation phase.[111]

Aside from restrictive financial measures, the G7 has pursued several multilateral investment initiatives since 2021. Supply chain security is a major theme, with Japan playing a leading role in defining economic security and setting an example for diversifying critical supply chains through international resource partnerships.[112] The US-led Minerals Security Partnership includes all G7 members and aims to coordinate investments in new critical mineral sources and supply chain-related infrastructure to diversify away from China. The EU and the United States unsuccessfully attempted to conclude critical minerals and sustainable steel and aluminum agreements in 2023. Despite this hiccup, bilateral investment coordination between G7 members has increased. Japan has concluded agreements on critical minerals with the United Kingdom and the United States.[113]

Many G7 initiatives have aimed to provide alternatives to Chinese development finance, such as the BRI. Since 2021, the G7's Partnership for Global Infrastructure and Investment (PGII), Just Energy Transition Partnerships (JETPs), and India-Middle East-Europe Economic Corridor (IMEC) have advanced plans to direct public or private investment to infrastructure projects in low- and middle-income countries. These initiatives rely on voluntary pledges from G7 members to raise funds and allow for varying degrees of commitment, easing the process of finding consensus among the partners. By the same token, the flexibility of these initiatives means the benefits are uncertain and subject to change depending on G7 members' commitment. Non-G7 partners also play an important role – for example, India in the IMEC proposal. Thus, these measures attempt to expand the G7's positive (geoeconomic) influence into new areas.

Interim Conclusion

The G7 shares many objections to China's human rights record, coercive economic behavior, aggressive territorial claims, and manipulation of global markets. G7 nations also face common risks vis-à-vis industrial espionage, supply chain disruptions, and anti-competitive behavior by Chinese firms. The G7 has served as a platform for focusing attention on these concerns. Human rights issues in Xinjiang, Tibet, and Hong Kong have been addressed – albeit to negligible effect – through visa bans and asset freezes coordinated among G7 members.

Yet the most significant geoeconomic actions against China have occurred unilaterally, with G7 buy-in as a follow-on effort.

The geoeconomic actions of G7 members against China's military have had poor results. The arms embargo instituted since 1989 has neither halted the modernization of China's military, nor has it prevented the direct sale of European components for Chinese weapons systems. In 2023, China cited US sanctions on its defense minister as a reason for refusing military-to-military talks that the United States said were crucial for avoiding unwanted accidents and escalations.[114]

Measures against Chinese telecom and semiconductor firms have seen some success. Following US export restrictions on semiconductors, with cooperation from Japan and the Netherlands, Chinese semiconductor imports by value fell 15.4 percent while imports by volume fell 10.8 percent. This data suggests that Chinese firms could be shifting toward less valuable – and less advanced – chips.[115] The Chinese government is reportedly planning to advance a state fund of $40 billion to invest in equipment for the domestic semiconductor industry.[116] While US sanctions on Chinese telecom firms reduced Huawei's annual

110 Peter Baker and David Sanger, "Biden Orders Ban on New Investments in China's Sensitive High-Tech Industries," *The New York Times*, August 9, 2024: https://www.nytimes.com/2023/08/09/us/politics/biden-ban-china-investment.html (accessed January 19, 2024).

111 Bounds, "EU Scales Back China Investment Screening Plans" (see note 107).

112 Joseph Rachman, "Japan Might Have an Answer to Chinese Rare-Earth Threats," *Foreign Policy*, August 15, 2023: https://foreignpolicy.com/2023/08/15/japan-rare-earth-minerals-green-transition-china-supply-chains/#:~:text=Japan%27s%20supply%20chain%20for%20these,supply%20of%20neodymium%20and%20praseodymium (accessed January 28, 2024); Osawa, "How Japan Defines Economic Security" (see note 88).

113 Department for Business and Trade, *UK-Japan Critical Minerals Memorandum of Cooperation*, October 28, 2023: https://www.gov.uk/government/publications/uk-japan-critical-minerals-memorandum-of-cooperation (accessed January 9, 2024); US Trade Representative, *United States and Japan Sign Critical Minerals Agreement*, March 28, 2023: https://ustr.gov/about-us/policy-offices/press-office/press-releases/2023/march/united-states-and-japan-sign-critical-minerals-agreement (accessed January 28, 2024).

114 Nike Ching, "State Department Clarifies: Not Lifting Sanctions on China's Defense Chief," *Voice of America*, May 22, 2023: https://www.voanews.com/a/state-department-clarifies-not-lifting-sanctions-on-china-s-defense-chief-/7104480.html (accessed January 28, 2024).

115 Debby Wu and Ailing Tan, "China Chip Imports Suffer Steepest Drop on Record After US Curbs," Bloomberg, January 15, 2024: https://www.bloomberg.com/news/articles/2024-01-15/us-china-chip-war-china-sees-biggest-drop-in-imports-on-record-in-2023 (accessed January 19, 2024).

116 Julie Zhu et al., "Exclusive: China to Launch $40 Billion State Fund to Boost Chip Industry," Reuters, September 5, 2023: https://www.reuters.com/technology/china-launch-new-40-bln-state-fund-boost-chip-industry-sources-say-2023-09-05 (accessed January 19, 2024).

net profit by nearly 70 percent in 2022,[117] Huawei's revenues stabilized in 2023. This development raises concerns that China could develop domestic chip alternatives.[118] Though export bans have undoubtedly damaged specific Chinese firms, such measures could plausibly slow China's technological development or accelerate the indigenization of key components in the medium to long term.

Investment screening policies have gained in popularity. The Biden administration has adopted the EU's "de-risking" language and advanced the most aggressive measures. On the other hand, many European firms have continued investing in China: Germany's FDI to China reached a record level in 2023.[119] The G7 remains divided on this issue, especially regarding outward investment screening.

G7 infrastructure and supply chain investment initiatives are largely too new to judge, and initial indications are uncertain. Multilateral JETPs with South Africa, Indonesia, Senegal, and Vietnam have already unlocked funds from G7 members but have run into political difficulties, especially in South Africa. Under the auspices of the PGII, the United States recently promised $250 million in development aid to Angola conditional on their selection of a European consortium over a Chinese competitor to build a railway that will deliver critical minerals to the Atlantic coast.[120] The Minerals Security Partnership shortlisted projects in June 2023 and could announce investments in 2024.[121] On the other hand, IMEC is struggling to move forward amid threats to Middle East security.[122] In addition, the stalled EU-US critical minerals and sustainable steel and aluminum agreements indicate that serious barriers remain to addressing supply chain issues through the G7.

The success and failure of the G7's geoeconomic initiatives against China follow from several factors:

- G7 members have vastly different economic dependencies on China. Canada, Japan, and the United States have relatively less dependence on China compared to the EU and especially Germany. While Japan has effectively de-risked and diversified its critical minerals supply chain and its major banks have only one percent of assets exposed to China, one million German jobs are directly dependent on trade with China.[123] France and Germany both held summits to support commercial ties with China in 2023.[124] Italy joined China's BRI to attract investment and trade before withdrawing in 2023.[125] Though China is a top trade partner for all G7 members, the "China exposure" of the United States – measured by total exports and firms' revenues from China – totaled 4.2 percent of GDP in 2020, compared to 2 percent for Italy, 5 percent for France, and 9.9 percent for Germany.[126] These diverging economic interests have undermined the G7's ability to impose sanctions on China and created friction among members.

- Threat perceptions of China have converged somewhat but remain different across the G7. Canada, Japan, and the United States have borne the brunt of aggressive Chinese behaviors in

117 Chang Che, "Huawei, Pummeled by US Sanctions, Reports Plunge in Profit," *The New York Times*, March 31, 2023: https://www.nytimes.com/2023/03/31/business/huawei-annual-earnings-2022.html (accessed January 19, 2024).

118 Zen Soo, "Huawei Reports its Revenue Inched Higher in January-September Despite US Sanctions," AP News, October 27, 2023: https://apnews.com/article/huawei-china-sanctions-revenue-smartphones-e9b26028fc748db364d279c5a5c2f705 (accessed January 19, 2024).

119 Sarah Marsh, "German Investment in China Rises to Record High," Reuters, February 14, 2024: https://www.reuters.com/markets/german-investment-china-rises-new-record-high-2024-02-14/ (accessed March 11, 2024).

120 US Department of State, *The United States and Angola: Partnering for Prosperity*, 2024: https://www.state.gov/the-united-states-and-angola-partnering-for-prosperity/#:~:text=The%20President%27s%20Partnership%20for%20Global,Atlantic%20Ocean%20through%20to%20Zambia; Mike Phillips, "How the US Is Derailing China's Influence in Africa," *Wall Street Journal*, January 21, 2024: https://www.wsj.com/world/africa/angola-africa-china-us-railroad-f0e23523 (both accessed January 28, 2024).

121 Attracta Mooney, "US-led Minerals Partnership Shortlists Projects for Green Energy Shift," *Financial Times*, June 14, 2023: https://www.ft.com/content/16927ddd-3cb9-4516-9934-eb94b032aea8 (accessed January 19, 2024).

122 Michelle Jamrisko and Alberto Nardelli, "World's Most Ambitious Trade Route Stalls in Mideast Turmoil," Bloomberg, January 23, 2024: https://www.bloomberg.com/news/articles/2024-01-23/world-s-most-ambitious-trade-route-stalls-in-middle-east-turmoil?cmpid%3D=socialflow-twitter-markets&utm_content=markets&utm_source=twitter&utm_medium=social&utm_campaign=socialflow-organic (accessed January 28, 2024).

123 Takaya Yamaguchi et al., "Exclusive: Japan Regulator Sounded out Top Domestic Banks about China Risks, Sources Say," Reuters, June 20, 2023: https://www.reuters.com/business/finance/japan-regulator-sounded-out-top-domestic-banks-about-china-risks-sources-say-2023-06-19; Melissa Eddy, "Germany Says China Trade Could Create Perilous Dependence," *The New York Times*, July 13, 2023: https://www.nytimes.com/2023/07/13/business/germany-china-trade.html#:~:text=That%20push%20created%20a%20tight,part%20of%20their%20supply%20chain (both accessed January 19, 2024).

124 Michel Rose and James Pomfret, "With Lavish Treatment of Macron, China's Xi Woos France to 'Counter' US", Reuters, April 7, 2023: https://www.reuters.com/world/with-lavish-treatment-macron-chinas-xi-woos-france-counter-us-2023-04-07 (accessed January 28, 2024).

125 Ilaria Mazzocco and Leonard Palazzi, "Italy Withdraws from China's Belt and Road Initiative," Center for Strategic and International Studies, December 14, 2023: https://www.csis.org/analysis/italy-withdraws-chinas-belt-and-road-initiative (accessed January 19, 2024).

126 "Europe Can't Decide How to Unplug from China," *The Economist*, May 15, 2023: https://www.economist.com/international/2023/05/15/europe-cant-decide-how-to-unplug-from-china; Eurostat, *China-EU – International Trade in Goods Statistics*, 2023: https://ec.europa.eu/eurostat/statistics-explained/index.php?title=China-EU_-_international_trade_in_goods_statistics (both accessed January 19, 2024).

military and diplomatic domains, while Japan and the United States have the most at stake in terms of Chinese territorial claims in the Asia-Pacific.[127] In the EU, leaders have taken a different approach, judging the security threats from China to be more distant than the economic benefits of Chinese trade. Though the Commission has adopted a firmer line, leaders in many member states hesitate to jeopardize commercial links with China.[128]

- Varying capacities among G7 members to create and enforce sanctions have influenced their ability to execute strategies together. Having coordinated and enforced the lion's share of UNSC sanctions against Iran, the United States has greater experience with sanctions. The close economic and security relationships of Canada and Japan with the United States create nearly irresistible incentives to align with US policy. The EU, on the other hand, is preoccupied with the Commission's attempt to unify sanctions and investment screening policies throughout the bloc. As a result, the United States launched sanctions against Chinese telecom and semiconductor firms unilaterally via executive orders and only later extended them to the G7 through bilateral agreements and the threat of secondary sanctions.[129] This institutional and legal asymmetry puts the United States in the driver's seat, while the G7 is reduced to a platform for coordination.

- Finally, (similar to the Russian case) the growing importance of the countries of the Global South and emerging markets has created additional risks to G7 coordination. While the G7 has sought to win support in the Global South, coordinated G7 activity there is often seen as an echo of colonial histories.[130]

127 Marian Seliga, "The European Union Not Willing to Risk Business with China," *East Asia Forum*, September 29, 2023: https://eastasiaforum.org/2023/09/29/the-european-union-not-willing-to-risk-business-with-china (accessed January 28, 2024).

128 Ibid.; Economist Intelligence Unit, *An EU-China Trade War is Brewing*, December 5, 2023: https://services.eiu.com/an-eu-china-trade-war-is-brewing (accessed January 19, 2024).

129 Gregory Allen and Emily Benson, "Clues to the US-Dutch-Japanese Semiconductor Export Controls Deal Are Hiding in Plain Sight," Center for Strategic and International Studies, March 1, 2023: https://www.csis.org/analysis/clues-us-dutch-japanese-semiconductor-export-controls-deal-are-hiding-plain-sight (accessed January 19, 2024).

130 Jonathan Josephs, "G7 Summit: Africa Seeks New Role as Nations Eye its Resources," BBC, May 19, 2023: https://www.bbc.com/news/business-65649834; Timur Fomenko, "The G7 is an Outdated Tool of the US Neo-Empire," RT, Azerbaycan, May 25, 2023: https://www.azerbaycan24.com/en/the-g7-is-an-outdated-tool-of-the-us-neo-empire

CONCLUSIVE ASSESSMENT

The G7 as a Geoeconomic Actor

As shown in the case studies on Russia, Iran, and China, the members of the G7 frequently employ geoeconomic strategies, including economic instruments, to defend and advance national economic and security interests (mostly) within the bounds of the rules-based international order. Yet is the G7 also a geoeconomic actor? How effective is the G7 in agreeing on and implementing geoeconomic strategies?

As mentioned in Chapter 1, a geoeconomic actor is characterized by the following traits: 1. It has a distinct set of values and clearly defined economic and security interests; 2. it has a vision or agenda for its own future as well as for the global economic and security order; 3. it can quickly and effectively adopt strategies that reflect changes in the geopolitical and geoeconomic environment; 4. it possesses a set of defensive and offensive instruments that can be readily employed to pursue said values, interests, and visions; and 5. it possesses the necessary political and economic weight to make these instruments meaningful.

Taking these characteristics – as well as the findings of the three case studies – into account, the picture for the G7 is mixed. There are five primary reasons for this:

1. LIMITS IN THE G7'S INSTITUTIONAL SET UP AND TOOL KIT

The setup of the G7 has become more formal over the decades. Yet, despite its many new working groups and procedures, it is far from being a fully-fledged international organization. The G7 does not have a secretariat. Its declarations are not legally binding under international law. Monitoring compliance with the declarations of the G7 is limited, and there is no formal enforcement mechanism.

Furthermore, the G7 does not possess joint instruments or institutions to implement its communiqués. There are no G7 export controls, investment screening mechanisms, sanctions, or trade defense instruments. Rather, the G7 members – at best – coordinate the application of their national instruments. Geoeconomic instruments regularly employed by G7 members, typically sanctions and export controls, are largely defensive in nature and limited in scope. The G7 has done little, for example, to coordinate trade defense instruments such as anti-subsidy or anti-dumping measures. The few examples of proactive, offensive instruments include joint announcements to invest in infrastructure to counter China's Belt and Road Initiative and improve supply chain resilience and security. These programs have had limited success so far.

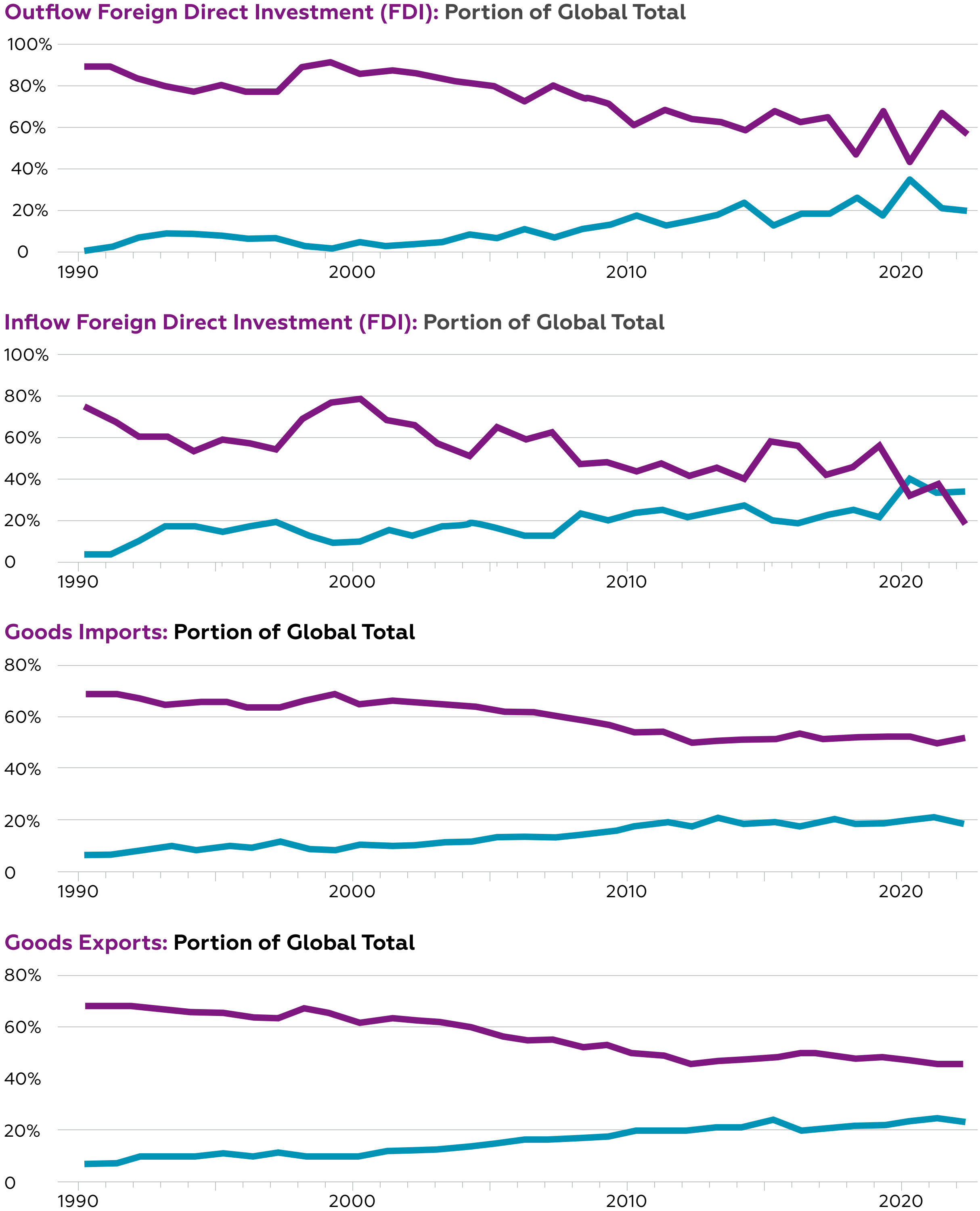
2. VARYING GEOECONOMIC CAPABILITIES

G7 members possess different capacities for deploying geoeconomic tools, most notably sanctions. While the United States has swiftly redeployed preexisting statutory authorities to target foreign entities, the EU often depends on the United States or the UNSC to craft sanctions packages. It has less experience developing its own sanctions, particularly at the Commission level. Since 2022, this has markedly improved regarding the sanctions packages against Russia. Still, key issues of enforcement are left to EU member states, which creates additional challenges. Other G7 members have adopted a similar approach, relying on US enforcement capacities. These institutional differences create significant mismatches in the ability of G7 members to adopt policies on a common timeline and with common enforcement mechanisms and durable political support.

3. DIVERGING DEPENDENCIES, RISK PERCEPTIONS, AND INTERESTS

While the G7 countries share many values, their interests are not always fully aligned. For instance, after Russia forcibly annexed Crimea in 2014, G7 members disagreed on the duration and conditions of sanctions. The fractious response reflected G7 members' differing economic interests, dependencies, and vulnerabilities, as well as different historical experiences, risk perceptions, and preferences for diplomatic solutions rather than hard sanctions. General discord between the transatlantic partners during the Trump administration also made G7 cooperation difficult, especially following the collapse of the JCPOA after the unilateral withdrawal of the United States. While the G7 has shown great unity countering Russia's 2022

6 – FDI Inflow/Outflow: G7 versus BRICS*

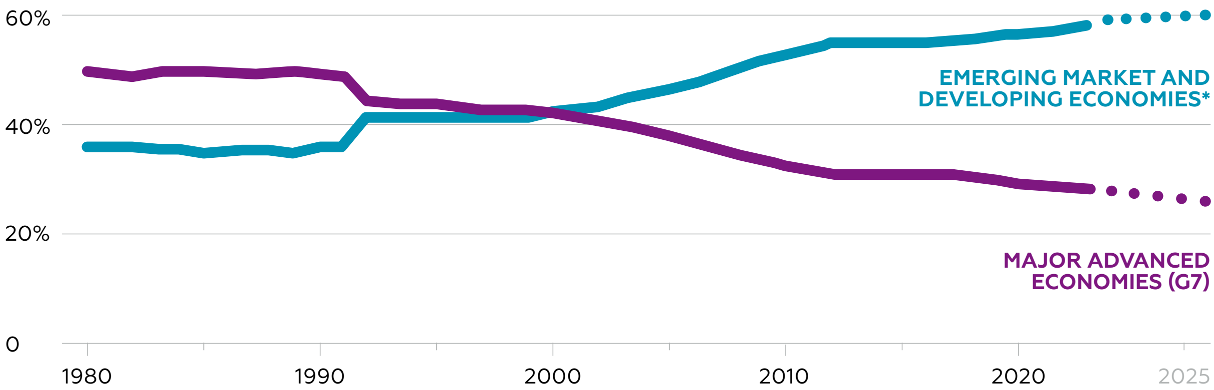


*Here, BRICS refers to the original grouping of countries: Brazil, Russia, India, China (including the special administrative regions of Hong Kong and Macao), and South Africa. It does not include recently added members. Also, please note that no figures exist for Russia from 1990 to 1991.

Source: Authors' own compilation based on UNCTADSTAT/US.FdiFlows, UNCTADSTAT/US.TradeMerchTotal

7 – Economic Weight of the G7

GDP Based on Purchasing Power Parity (PPP), Share as Percent of World



*The term "Emerging Market and Developing Economies" refers to 195 countries that are not included in the IMF's "Advanced Economies" category in its World Economic Outlook datasets. All G7 members are considered "Advanced Economies" while all BRICS members are considered "Emerging Market and Developing Economies."

Source: IMF

invasion of Ukraine, G7 members are cautious to completely sanction the country because that would cause energy prices in Europe and Japan to skyrocket. This caution is even more apparent in the case of China, given its importance for the world economy. Furthermore, the G7 members continue to diverge in their implementation of export controls and investment screening measures toward China. Again, differing economic interests, dependencies, and risk perceptions have prevented a more concerted approach – despite the small degree of greater alignment that can be observed recently.

4. DIFFERENCES IN TACTICS AND STRATEGIES

Even when G7 members share the same objective, they sometimes differ in their strategies and tactics. A case in point is the approach toward Iran. Based on the G7's shared concern for human rights and support for nuclear non-proliferation, Iran is an area of robust G7 cooperation – apart from some exceptions. The primary difference within the G7 involves strategy not objectives. The group has diverged between the "maximum pressure" campaign of the United States under President Trump and the EU and Japan's diplomatic and economic outreach. These differences are also tactical and measure-specific: Canada, the EU, and the United Kingdom have generally adopted sanctions targeted at listed individuals and entities, whereas the United States has targeted entire industries and, in some cases, almost the entire Iranian economy.

5. DECREASING ECONOMIC AND POLITICAL CLOUT

Lastly, the G7 is still an economic and political powerhouse and has considerable influence over global security and economic governance. However, its decreasing share in global gross domestic product (GDP), trade, and investment has and will continue to reduce the power of its geoeconomic instruments. While the G7 still accounted for 65 percent of global GDP in 2000, this share had fallen to 44 percent in 2021. The seven largest emerging economies (E7: Brazil, China, India, Indonesia, Mexico, Russia, and Turkey) are expected to overtake the G7 in economic size during the 2030s. China could also become the world's largest economy in the 2030s.[131] Given the changing nature of the global economy and the economic weight of the Global South, G7 sanctions and export controls can be circumvented more easily. Two cases in point are the recent circumvention of sanctions on Iran and Russia and the changing nature of value chains. Loopholes, enforcement, and circumvention are again proving to be serious stumbling blocks in making sanctions or the Russian oil price cap more effective.

131 UK Government, *Global Trade Outlook*, February 2023, p. 29: https://assets.publishing.service.gov.uk/media/63fcd76de90e0740df9e0315/global-trade-outlook-february-2023.pdf (accessed January 4, 2024).

RECOMMENDATIONS

The Future of the G7 Alliance

Given the changing geopolitical and geoeconomic environment, demands for the G7 to engage as a geoeconomic actor are likely to increase. It remains to be seen whether Russia's war on Ukraine, China's striving for global influence, the war between Israel and Hamas, or Iran's conflictual role in the Middle East will be uniting factors that will help the G7 to overcome differences in risk perceptions as well as political and economic interests. The presidential and congressional elections in the United States in November 2024 will be a decisive factor – as will the European elections in June 2024 and their impact on the next European Commission. What's clear: G7 members must act more quickly and decisively to apply defensive geoeconomic instruments, cooperate more closely on enforcement and preventing circumvention, and act more proactively by expanding available offensive instruments. In light of economic power shifts toward emerging economies, the members of the G7 need to redouble their efforts to persuade democratic countries like India and Brazil to join G7 measures or at least not undermine them.

Against this background, we have the following six recommendations for the G7 alliance:

1. ALIGN THE INTERESTS AND RISK PERCEPTIONS OF G7 MEMBERS

The G7 has struggled to find consensus on geoeconomic measures that demand significant economic sacrifices – for example, de-risking measures against China. In these cases, the G7 must find a common position on the risks faced by the bloc that might justify such sacrifices. To do so, the G7 should embrace new information-sharing platforms, including crisis scenario exercises and joint vulnerability studies in key sectors. Though members could be hesitant to share sensitive information, these exercises would present opportunities to build resilience and trust as well as share risk perceptions, thus aligning interests. This is especially important for the EU, which must cultivate an economic "risk culture" among its member states to reduce differences in risk perception and enable more coherent geoeconomic policies.[132]

2. EXPAND COORDINATION THROUGH G7 WORKING GROUPS

In recent years, fissures within the G7 have resulted from the differing speeds at which members can decide and implement geoeconomic policies. A more functional approach would see the United States collaborate with other G7 members during the policymaking process, perhaps through more formalized working groups at the cabinet or sub-cabinet level between ministries that issue regulations, grants, and other measures relevant to geoeconomic objectives. At the same time, working groups could improve the ability of G7 members to propose and enact geoeconomic measures rather than simply follow the lead of the United States. An expansion of working groups – building on the existing non-proliferation directors and finance ministers groups to cover the full breadth of G7 topics – could reduce time lag between decision-making by the G7 and implementation by its members, thereby establishing an institutional framework for developing coordinated policies that can be implemented by all G7 countries.

The expanded working groups should reflect the broadening of the G7's agenda from financial stabilization to sanctions coordination, investment programs, trade restrictions, technology, and defense. Models could include the EU-US Trade and Technology Council (TTC), NATO's sub-regional groupings, and the Ukraine Defense Contact Group.[133] Similarly, the EU should also adopt institutional reforms to create a "one-stop shop" for coordination between member states and engagement with G7 partners on geoeconomic issues.[134]

132 Elvire Fabry et al., "Shields Up," p. 27 (see note 96).

133 Neil Melvin, "Episode 54: The US and the Future of European Security," Royal United Services Institute, July 12, 2023: https://www.rusi.org/podcasts/global-security-briefing/episode-54-us-and-future-european-security (accessed February 12, 2024).

134 Fabry et al., "Shields Up," p. 27 (see note 96).

3. IMPROVE THE GEOECONOMIC CAPABILITIES OF G7 MEMBERS

The G7 has traditionally relied on the United States to craft and enforce punitive measures, especially financial sanctions. Yet the US withdrawal from the JCPOA revealed the extent to which political decisions in Washington can rupture the entire G7's strategy and ability to create effective geoeconomic policies. G7 members must view the development of independent geoeconomic capabilities as a means to enhance credibility. In the EU, this will require resolving gaps between member states in export control enforcement and investment screening. Canada, Japan, and the United Kingdom must determine which independent capabilities can be built, and which will require ongoing codependency with the EU or United States. In a positive scenario, additional leadership from G7 partners would address US criticism regarding burden-sharing while insulating the G7 from sudden shifts in US policy.

4. SET JOINT STANDARDS FOR NEW DISRUPTIVE TECHNOLOGIES

The G7 countries – individually and within organizations such as NATO or international standard setting bodies – are working on technical standards and norms for new and disruptive technologies. In doing so, the G7 could play a more active role in preparing the ground for establishing international principles of responsible use. A model for this could be the G7 Hiroshima AI Process. The Hiroshima AI Process Comprehensive Policy Framework, on which the G7 had agreed under Japan's G7 Presidency, is the first international framework that includes guiding principles and a code of conduct. It is aimed at promoting safe, secure, and trustworthy advanced AI systems. Following this example, the G7 could identify priority technology areas for which guiding principles and a code of conduct should be developed.

5. ENHANCE INVESTMENT INITIATIVES

If they are funded sufficiently and made effectively, investments could play a key role in promoting partnerships that would expand the G7's influence and advance its global development goals. However, the G7 must progress from the current phase – in which new investment initiatives are frequently launched – to a more established phase with stable financing and clear-cut strategies.

Some investment initiatives, such as the JETP, already have a secretariat. Yet others must rely on a G7 member to provide structure, as the Triple I for Public Health Initiative does with Japan. Given the political and financial complexities of coordinating activities among the G7 and partners from the private sector and non-G7 countries, these secretariats should be scaled up to provide financial accountability and political expertise. In some cases, formal partnerships with multilateral development banks would be valuable, particularly in the regions where projects take place. The G7 should also conduct appropriate outreach to civil society to ensure investments have long-term support, to foster positive outcomes for all members of that society, and to improve the appeal of G7 initiatives compared to China's development programs.

6. INCREASE PARTNERSHIPS WITH DEVELOPED DEMOCRACIES AND THE GLOBAL SOUTH

The G7 should respond by deepening partnerships with other developed democracies as well as the countries of the Global South that share G7 values or objectives. Australia and South Korea, for example, have emerged as significant supporters of Ukraine and partners in semiconductor export controls against China.[135] Many countries of the Global South are not interested in being part of a China or Russia camp, but aim for fair access to other markets, technology, resources, etc. Beyond fully-fledged expansions of the alliance, pursuing discussions on topics of concern for developing and emerging economies – for instance, debt refinancing, resource partnerships, and sustainability – will help build durable relationships. These could be institutionalized through topic-specific clubs that invite non-G7 members to help lead certain initiatives. Crucially, the G7 must demonstrate the value of its partnerships to emerging economies to expand its influence and remain a relevant partner. The G7 should view itself not as a "steering committee" for the West, but as a platform where developed democracies and emerging economies can boost their commercial and diplomatic ties through initiatives that unite around shared challenges.

135 Ronald Klain, "It's Time for the G9," Carnegie Endowment for International Peace, November 9, 2023: https://carnegieendowment.org/2023/11/09/it-s-time-for-g9-pub-90969 (accessed February 11, 2024).

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