SPECIAL REPORT

Economic coercion
Boycotts and sanctions—preferred weapons of war

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About the author

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EXECUTIVE SUMMARY

Economic coercion is increasingly being used unilaterally as a tool of foreign policy, and sanctions, technology controls, boycotts and arbitrary regulation are introducing new risks for business. At the global level, the unilateral exercise of coercion devalues the rules of global commerce set out by the World Trade Organization in favour of economic relations governed by the exercise of power.

Many nations, including Australia, have the ability to impose sanctions that go beyond those ordered by the UN. However, only the most powerful nations are able to unilaterally constrain the economic choices of others.

China has a long history of restricting access to its vast market as a means of economic coercion, while the US has built an armoury of coercive tools, including national and individual sanctions, export controls and investment restrictions. As the controller of the most widely used global currency, the US is able to constrain the financial transactions of its targets.

While Australia is highly unlikely to be a target of US sanctions and is also likely to implement parallel sanctions where national interests align, for Australian firms, the increasingly aggressive deployment of economic coercion by the US poses a risk of collateral damage and demands a much more rigorous approach to compliance.

The Australian Government has been a focus of threats from Chinese Government officials and state media in recent years, and real economic coercion has been directed against particular trade sectors and companies. For organisations trading with China, there’s a risk of becoming a target and suffering material losses. There are 14,000 Australian firms selling to China either directly or through Hong Kong, while a much larger number of businesses, including many thousands of farm enterprises, depend on the Chinese market through intermediaries.

Economic coercion has its place in the foreign policy toolkit as a response to acts of aggression or threats to international security that fall short of war. With broad backing, it can be effective. The imposition of UN sanctions on Iran in 2006, with support from the US, Europe, Russia and China, helped push Iran to negotiate over its nuclear program.

However, economic coercion is ultimately a contest of resolve on both sides. The nation imposing coercion seeks to demonstrate its determination to prevail on the strategic or policy objective that it’s pursuing, while the target often rallies nationalist supporters—or even international partners—to fend off the economic pressure to comply.

The academic literature gives economic coercion a poor record of success, at least when it comes to formal sanctions achieving big, set-piece outcomes. The example of Cuba, which has endured six decades of US economic sanctions without the least shift in policy, is frequently cited. However, success can be difficult to measure. The pain Cuba has suffered may have discouraged other leftist Latin American governments from expropriating US property.

The imposition of sanctions on Russia over its annexation of Crimea might not have persuaded it to withdraw, but might have discouraged further incursions into Ukraine.
The use of economic coercion has become much more frequent over the past three years. The Trump administration has seen it as a cheaper alternative to military intervention and has been more willing to act unilaterally. Although the administration has focused on ‘pariah’ nations such as Venezuela, Iran and North Korea, it has also taken sweeping action against Russia and is under pressure from both sides of Congress to take stronger action against China on human rights grounds.

China’s exercise of coercion has been less focused. Prominent targets over the past decade have included Japan, South Korea and France. However, where there’s a significant imbalance of power and where the prospect of retaliation is slight, smaller nations have been the most frequent targets. One study counted 22 separate exercises of coercion by China against its neighbours in the South China Sea over the decade to 2015, while an ASPI report on Chinese coercive diplomacy counted 152 instances involving 27 countries over the past decade. China has also aimed at individual corporations active in the Chinese market, seeking to condition their behaviour.

The spread of China’s targets has widened, and the Covid-19 crisis has generated a spate of threats, including against Australia, Sweden, the UK, the Czech Republic, Germany and the Netherlands.

The growing use of economic coercion demands that Australian businesses with international operations be more aware of the strategic issues affecting their clients, suppliers and financial counterparties. In making any ventures into the Chinese market, they should act with their eyes open to the potential risks.

Australia is a mid-sized economy, so our national interest is served by a global trading environment governed by clear rules backed by independent institutional enforcement. Yet, as Prime Minister Scott Morrison has warned, the world is becoming poorer, more dangerous and more disorderly. It’s an environment in which economic relations are no longer governed by trust and law. Australia will always be a loser in a world where economic relations are governed by the exercise of power.

However, the resort to coercion is rising at time when the multilateral institutions and forums to moderate conflict between nations are losing their force. Both sides of US politics harbour deep reservations about the World Trade Organization, while the G20 has failed to provide effective leadership during the Covid crisis.

This report examines first the tools of economic coercion, with sections examining the growing use of sanctions and the more informal boycotts and regulatory punishments imposed by China.

The report then looks at the effectiveness of economic coercion, which is shaped partly by the clarity and realism of the objectives, given conditions in the target country. However, it’s also critically shaped by the perceptions of the legitimacy of the coercive action in the target country and by the resolve of its government and the companies involved to withstand economic pressure.
Recommendations

- Economic coercion is part of the commercial reality that internationally engaged businesses and organisations such as universities and NGOs must deal with. They need to be attuned to the national security and political risks of their upstream and downstream counterparties, and how those risks may be growing or changing.

- With the growing politicisation of trade, there’s a case for the Australian Government to include the Trade Minister in the National Security Committee of Cabinet to ensure that they embark on any trade negotiations fully aware of national security priorities and that the direction of national security policy is decided in full awareness of the economic consequences.

- The potential for China to apply economic boycotts or other forms of coercion should be incorporated into the planning of any organisation aiming to sell into that market. That threat can be unpredictable, and organisations might be made liable for the words or deeds of their government, which constitutes a sovereign risk.

- Businesses can’t expect the Australian Government to compensate them for sovereign risk, but the government could choose to offer structural adjustment packages to assist affected sectors to diversify their markets as a demonstration of its resolve to resist coercive pressure.

- The Australian Government should be prepared to call out attempts by China to exercise coercion through actions against individual companies and organisations and should provide business with representative support and guidance. The key to resisting economic coercion is national resolve, and the government should make that the heart of its communications response.

- Organisations with international exposure should maintain sanctions compliance programs to ensure that they don’t inadvertently trigger any breaches. In addition to the sanctions imposed by the major powers, by the UN and by Australia, businesses should be aware of their obligations set out by the Financial Action Task Force governing money laundering and the financing of terrorism. The US Office of Foreign Assets Control publishes helpful guidance on what it considers to be an adequate sanctions compliance program.

- Australian business is unlikely to take the threat of economic coercion seriously in the absence of a respected regulator. The regulation of sanctions is inappropriately housed within the Department of Foreign Affairs and Trade. It would make more sense for that responsibility to be shifted to the finance regulator, AUSTRAC.

- Although economic coercion has its place in the foreign policy toolkit in response to acts of aggression and threats to international peace, it’s being overused in an environment in which economic conflict is being normalised. Australia’s national interest is in the good governance of international economic relations with universally respected rules and forums for mediating differences.

- International forums such as the G20, Asia-Pacific Economic Cooperation, the Organisation for Economic Co-operation and Development and the World Trade Organization (WTO) should be concerned about the growing use of economic coercion, which is a threat to the freedom of commerce.

- The Australian Government should be ready to use the WTO to dispute the use of coercive measures against Australian exporters and should oppose the widening use of the WTO’s national security exemptions from the normal rules of free trade.

- The Australian Government should strongly endorse the WTO and the rules-based framework that the WTO administers as the foundation for global commerce.
In his major foreign policy speech ahead of the 2016 US presidential election, Donald Trump declared that, unlike other candidates for the presidency, ‘war and aggression will not be my first instinct.’ Rather, he said, ‘financial leverage and sanctions can be very, very persuasive but we need to use them selectively and with total determination.’

After 15 years of intense warfare in Iraq and Afghanistan, which had followed a decade of intermittent Middle East combat since the 1990 Gulf war, America was tiring of overseas military expeditions. Trump promised he could achieve his foreign policy objectives without shedding either the blood of US soldiers or the treasure of taxpayers.

Trump’s words echoed those of Woodrow Wilson, US President from 1913 to 1921, who, in 1919, looked to a world in which war would be rendered obsolete. ‘A nation that is boycotted is a nation that is in sight of surrender. Apply this economic, peaceful, silent, deadly remedy and there will be no need for force,’ he said.

Wilson had been impressed by the effectiveness of the British naval blockade of the North Sea and the English Channel during World War I, which had effectively deprived the German economy of foodstuffs and raw materials, leading to widespread rioting in German cities from 1916 onwards (Figure 1). ‘This war was won not only by the armies of the world. It was won by economic means as well,’ he said. Although contemporary historians attribute Germany’s 1918 surrender to its inability to keep its war machine going after catastrophic losses on the battlefield, it was widely believed in the immediate aftermath, including by Wilson, that the English blockade had achieved what the trench-bound soldiers had failed to accomplish.

Blockades and sieges are at least as old as walled cities, but Wilson’s conviction about their efficacy led to the structure of economic sanctions deployed today by the UN, the US and other advanced nations, including Australia. Wilson laid the legal foundations in 1917 with the Trading with the Enemy Act, which, with amendments, is still the basis for much of US economic coercion. He also contributed to the inclusion of a sanctions power in the articles of the League of Nations, which was replicated after World War II under the UN.
China’s approach to economic coercion is different. It relies on informal boycotts and regulatory interventions, rather than formal sanctions or systematic export controls. It usually aims to restrict access to the vast Chinese consumer market. China almost always denies any political or policy intent while making certain that the target knows what infraction they have committed.

The use of consumer boycotts as a means of economic coercion runs deeply in China’s history; the first academic study of its practice was published by the American Academy of Political and Social Science in 1930. Written by political economist Dorothy Orchard, that paper charted China’s use of boycotts, starting with a well-coordinated ban on purchases of US goods in 1905 in protest against barriers to Chinese immigration, followed by a series of boycotts of Japanese goods starting in 1908 and, later, boycotts against British goods. The essence of China’s successful use of boycotts, the article said, ‘has rested upon the economic dependence of the boycotted nations upon China and China’s relative independence of them’.

The informality of the Chinese system of economic coercion and lack of accountability encourage potential targets to comply strictly with what they perceive to be China’s expectations.

By contrast, the US system of economic coercion is highly formalised. The Office of Foreign Assets Control, which is an agency of the Treasury Department, is in charge of administering the US system of economic sanctions imposed on nations, organisations and individuals. The Commerce Department’s Bureau of Industry and Security administers the increasingly important export controls.
The use of coercion has been a feature of international economic relations throughout the postwar period. Sanctions were a defining element of the Cold War: the US prohibited US exports to the Soviet Union from 1948 and to China and North Korea from 1950.

But the US always faced the problem that its own firms would suffer a loss of business to competitors, usually from Europe. The US attempted to force other nations to follow its lead with the 1951 Mutual Defense Assistance Act, which ruled that nations exporting goods of strategic importance, including oil, to the Soviet Union would be denied any US assistance; however, under protests from allies, exemptions were granted.

The UN sanction power, which represents the will of the international community, was little used until 1990. The Soviet Union exercised its veto power over sanctions that the US wished to pursue, while the UK vetoed sanctions against South Africa until 1977, when a limited arms embargo was imposed. Until the 1990s, Rhodesia was the only country to face comprehensive UN sanctions.

The US won UN backing for sanctions against Iraq following Iraq’s 1990 invasion of Kuwait, and that was the beginning of a much more activist era. While the sanctions on Iraq fell squarely within the UN’s Article 41, which said sanctions could be imposed to counter ‘acts of aggression’, UN sanctions were imposed for human rights abuses in Angola, Rwanda and the former Yugoslavia, as well as for support for terrorism in other nations. The UN currently has 14 sanction regimes, up from eight in the 1990s and 12 in the first decade of the 2000s.

The unilateral use of economic coercion by the US has accelerated dramatically under the Trump administration. While the informal nature of China’s exercise of coercion makes it harder to track, independent analysis shows that there’s been a clear increase in Beijing’s use of economic threats since the beginning of the Covid crisis, while the past three years have brought coercive actions against Australia, Canada, Taiwan, South Korea, Mongolia and the microscopic Pacific island of Pilau, among others.

This increasing resort to economic coercion is occurring as international economic relations generally have become more fractious (Table 1). The open embrace of globalisation from the mid-1980s through to the global financial crisis in 2007–08 has given way to a new economic nationalism. The pandemic’s exposure of vulnerabilities for many nations in getting essential medical supplies seems to be accelerating this trend. That’s most obviously true of the US and China, but is evident more broadly. In a world in which economic conflict has been normalised, economic coercion is an easier step to take.
Table 1: International trade sanctions

<table>
<thead>
<tr>
<th>Country</th>
<th>UN*</th>
<th>US*</th>
<th>Australia*</th>
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<td>Balkans</td>
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<td>Belarus</td>
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<td>Burundi</td>
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<td>Central African Republic</td>
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<td>Crimea</td>
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<td>Cuba</td>
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<td>Darfur</td>
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<td>Democratic Republic of the Congo</td>
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<td>Guinea Bissau</td>
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<td>Iran</td>
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<td>Iraq</td>
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<td>Lebanon</td>
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<td>Libya</td>
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<td>Mali</td>
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<td>Myanmar</td>
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<td>Nicaragua</td>
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<td>North Korea</td>
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<tr>
<td>Russia</td>
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<td>Somalia</td>
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<td>South Sudan</td>
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<td>Sudan</td>
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<td>Syria</td>
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<tr>
<td>Venezuela</td>
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<td>Yemen</td>
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<td>Zimbabwe</td>
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<td>Taliban</td>
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<td>ISIL/Al Qaeda</td>
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*a Since 2004, UN sanctions have been levied against individuals and organisations rather than governments.
*b The US doesn’t publish a separate list of countries with targeted sanctions, as sanctioned individuals and entities can change their locations.
*c Australian autonomous sanctions. Australia also implements all UN sanctions.
The Chinese Ambassador’s words were carefully chosen:

The Chinese public is frustrated, dismayed and disappointed with what Australia is doing now. I think in the long term … if the mood is going from bad to worse, people would think ‘Why should we go to such a country that is not so friendly to China?’ The tourists may have second thoughts.

The parents of the students would also think whether this place which they found is not so friendly, even hostile, whether this is the best place to send their kids here. It is up to the people to decide. Maybe the ordinary people will say ‘Why should we drink Australian wine? Eat Australian beef?’

Cheng Jingye is in the top echelon of China’s diplomatic service, having been posted to Australia in 2016 after assignments as Ambassador to the UN’s office in Vienna and as head of the Foreign Affairs Ministry’s arms control office. He was voicing the Chinese Government’s anger over the Australian Government’s call for an international inquiry into the origins and management of the Covid-19 pandemic that would be independent of the World Health Organization. Cheng characterised the inquiry proposal as part of a Washington-led ‘political campaign against China’.

While the ambassador’s comment could be read as a simple speculation about the reaction of patriotic Chinese citizens, Australian Foreign Minister Marise Payne viewed it as a threat. ‘We reject any suggestion that economic coercion is an appropriate response to a call for such an assessment, when what we need is global cooperation,’ she said.

The ambassador’s interview was followed in quick succession by the removal of Chinese certification for four Australian meat processors, the imposition of punitive tariffs on Australian barley exports to China, advice from China’s tourism ministry that anti-Chinese racism made Australia unsafe for Chinese tourists and similar advice from the Ministry of Education for students contemplating study in Australia. In addition to this economic retribution, China sentenced a convicted Australian drug smuggler to death.

China’s Ministry of Foreign Affairs denied that any of those actions represented economic coercion. Its spokesman, Geng Shuang, said that Ambassador Cheng had merely commented that Australia’s words and deeds had upset the Chinese people and that that may affect bilateral relations. ‘Is there any problem with that? How could it have anything to do with “economic coercion”?’ he asked.

The beef processors, one of which is Chinese owned, had been in a long and technical dispute over labelling and consignment certificates, which had resulted in a previous suspension in 2017. The barley tariffs were the culmination of a long investigation and were seen by some as retaliation for Australia imposing anti-dumping tariffs on Chinese steel.
A series of news reports about racist attacks on Asian people in Australia following the outbreak of Covid-19 were inflaming anti-Australian sentiment in Chinese social media. Individually, the actions all seemed explicable, but, collectively, the message was clear. As Perth USAsia Centre research director Jeff Wilson commented, ‘if you threaten to shoot someone, no one will believe when you stand over his body a week later and claim he accidentally fell on a bullet—of course it’s linked.’

The denial of official orchestration is a constant feature of Chinese coercion. The target can’t negotiate the economic punishment if no one is taking responsibility for inflicting it. The lack of any formal system for imposing coercive measures leaves potential targets second-guessing and pre-empting action by complying with China’s priorities. In a way, then, that informality gives China’s approach more influence over a wider range of actors beyond those directly targeted in any particular case.

Boycotts of goods or services are easily triggered, as the Chinese state displays an ability to turn on or off the tap of economic nationalism, which flourishes in Chinese social media. France, Japan and South Korea have all seen their national motor vehicle brands suffer disastrous plunges in Chinese sales after arousing the anger of Chinese authorities.

As well as consumer boycotts, China frequently uses the regulatory power of the state to inflict economic pain. The recent experience of meat processors mirrors the difficulties faced by Australian wine exporters in 2018 and thermal coal exporters in 2019 in gaining customs clearance for their Chinese sales.

One of the most coordinated Chinese coercive campaigns was undertaken against South Korea following its 2017 decision to allow the US to install an anti-missile system on its territory. Although the system was ostensibly designed to defend South Korea against a North Korean nuclear attack, the Chinese military believed that the system’s radar was aimed at it.

The Chinese state tourist authority banned tours to South Korea, which came to an abrupt halt when total Chinese tourist numbers halved. The South Korean supermarket chain, Lotte, which allowed one of the missile installations on one of its golf courses, had 70% of its branches in China shut down, ostensibly for breaching fire regulations, while it was heavily fined over alleged advertising practices. The company ultimately walked away from its US$6 billion investment in the Chinese market. Hyundai sales fell by nearly two-thirds.

Even then, Chinese officials denied any state-organised coercion. When South Korea raised the issue at a council meeting of the WTO, China’s delegate objected, saying ‘China was not aware of the existence of the “measures” mentioned by Korea, and regretted that Korea had raised the issue.’

A striking feature of the campaign against South Korea was the targets chosen: motor vehicles, tourism and supermarkets. Chinese consumers can easily buy cars other than Hyundais, travel in tour groups to somewhere other than South Korea or shop in supermarkets other than Lotte’s. China imposed no boycott on Korean semiconductors or capital equipment—indeed, its total imports from South Korea rose in 2017.

Similarly, it was easy for China to target Australian barley and beef, as it was already trying to accommodate greater US purchases under its bilateral trade deal. Students and tourists can go elsewhere, but China wouldn’t consider cutting back its purchases of Australian iron ore, which is an essential industrial input.

Ketian Zhang, in an analysis of China’s coercion against its neighbours in the South China Sea, concluded that coercion was deployed when the economic cost to China was low and the need to establish a reputation for resolve was high.

Zhang noted that the toughest action was taken against weaker countries in order to deter others. As the Chinese saying goes, ‘kill a chicken to scare the monkey’.
Coercion was little used between the late 1990s and 2007 because China was trying to get admitted to the WTO and then strike trade deals with ASEAN neighbours, so the economic cost was too high. Its determination to assert its sovereignty in the South China Sea has increased since then, while the economic cost of its actions has fallen.\textsuperscript{12}

Chinese coercion is frequently used to choke criticism of the Chinese Communist Party or departures from its authorised script on issues such as Taiwan or Hong Kong. Small targets invite harsh punishment. The Marriott hotel chain had its Chinese website taken down after an online customer survey implied that Tibet, Taiwan, Hong Kong and Macau were separate nations and had to publish an abject apology in its place. The message wouldn’t have been lost on any other travel businesses. The goal isn’t so much to change the behaviour of the target (in this case Marriott) as to change the behaviour of the entire industry.

The outbreak of coercive threats and actions in 2020 reflects China’s determination that the Covid-19 pandemic shouldn’t be used against it. Australia’s call for an independent inquiry into the pandemic and its urging that the World Health Organization should have unilateral intervention powers equivalent to those of weapons inspectors threatened the Chinese Government’s control of the Covid-19 narrative and potentially exposed its missteps in enabling the coronavirus to escape control.

Table 2: High profile cases of Chinese economic coercion since 2008 and the issues that triggered it

<table>
<thead>
<tr>
<th>Year</th>
<th>Country</th>
<th>Product</th>
<th>Reason</th>
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<tbody>
<tr>
<td>2008</td>
<td>France</td>
<td>Cars and supermarkets</td>
<td>Interruption to Olympic torch relay</td>
</tr>
<tr>
<td>2010</td>
<td>Japan</td>
<td>Rare earths</td>
<td>Arrest of Chinese fishing boat</td>
</tr>
<tr>
<td>2010</td>
<td>Norway</td>
<td>Salmon</td>
<td>Award of Nobel Prize to Liu Xiaobo</td>
</tr>
<tr>
<td>2012</td>
<td>Japan</td>
<td>Motor vehicles</td>
<td>Japanese Government purchases one of the Senkaku/Diaoyu Islands</td>
</tr>
<tr>
<td>2016</td>
<td>Philippines</td>
<td>Mangoes and bananas</td>
<td>Permanent Court of Arbitration confirms Philippines’ South China Sea rights</td>
</tr>
<tr>
<td>2017</td>
<td>South Korea</td>
<td>Tourism, cars, supermarkets</td>
<td>Installation of US anti-missile system</td>
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<tr>
<td>2017</td>
<td>Palau</td>
<td>Tourism</td>
<td>Pressure to switch recognition from Taiwan</td>
</tr>
<tr>
<td>2018</td>
<td>Australia</td>
<td>Coal</td>
<td>Foreign interference legislation and ban on Huawei</td>
</tr>
<tr>
<td>2019</td>
<td>Canada</td>
<td>Canola</td>
<td>Arrest of Huawei finance director</td>
</tr>
<tr>
<td>2019</td>
<td>United States</td>
<td>NBA basketball</td>
<td>Club official’s support for Hong Kong protests</td>
</tr>
<tr>
<td>2020</td>
<td>Australia</td>
<td>Barley, beef, wine, milk</td>
<td>Australian call for independent inquiry into Covid-19 origins</td>
</tr>
<tr>
<td>2020</td>
<td>Czech Republic</td>
<td>Skoda cars, Home Credit Group</td>
<td>Czech politician visiting Taiwan</td>
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<tr>
<td>2020</td>
<td>United Kingdom</td>
<td>Construction of nuclear plant, high-speed rail</td>
<td>UK ban on Huawei and offer of residency to Hong Kong’s British passport holders</td>
</tr>
</tbody>
</table>

Note: This list doesn’t include numerous actions against individual companies or South China Sea conflicts. For a comprehensive listing, see Fergus Hanson, Emilia Currey, Tracy Beattie, The Chinese Communist Party’s coercive diplomacy, ASPI, Canberra, August 2020, online.

Although the strategic and economic tensions between China and the US have become the dominant cleavage in international relations over the past three years, China has been careful in its use of coercive measures against the US.

A number of US companies have been affected. There’s been a consumer boycott of Apple in retaliation for the US campaign against Huawei. When the US placed Huawei and ZTE on an ‘entity list’, which barred them from receiving US technology, China declared that it had compiled an ‘unreliable entity list’, which would punish US companies that failed to meet sales contracts. The list was never released or acted on as negotiations on a US trade deal progressed.

There were also veiled threats in 2019 that China may withhold sales of rare earth minerals to the US, as it had done against Japan in 2010. Again, there was no follow-through.
Economic coercion can be effective only if there’s an imbalance of power. China can’t hope that the exercise of economic coercion against the more powerful US would deliver any change in policy. China’s major response to the US actions against Huawei has been directed at Canada, which arrested Huawei’s finance director, Meng Wanzhou, at the request of the US.

Canada’s sales of canola to China have been hit, while the luxury outdoor clothing brand Canada Goose has suffered a steep fall in Chinese sales. China has also charged two Canadians with spying and imprisoned them, while it has also sentenced a Canadian drug smuggler to death.

Australia’s alliance with the US may render it vulnerable to further Chinese coercive action as a weaker surrogate for the real source of Beijing’s anger. However, our pursuit of our own perceived national interest on topics ranging from Huawei to foreign investment and the scope of an inquiry into the pandemic has been sufficient to rouse Chinese threats and coercion. China’s presentation of Australia as the US’s junior partner seeks to blunt the broader international influence of the positions that Australia takes.
While China’s use of coercion is calculated to cause pain to selected industries or sectors in a target country, US sanctions are usually about seeking major change in a targeted nation’s strategic or military approaches. For that reason, US sanctions seek to damage the entire economies of some of the nations that Washington targets, making it as difficult as possible for them to trade with anyone.

Relative to the direct threat posed to Australian business by Chinese coercive action, the danger from US sanctions appears to be oblique. US action has been harshest when dealing with ‘pariah’ countries such as North Korea, Venezuela, Iran and Cuba, with which Australian organisations have little trade.

However, the severity and reach of US actions mean that Australian firms can be at risk of collateral damage. Incitec Pivot (a leading Australian chemicals and explosives company) has, since 2013, had an explicit company policy prohibiting the breach of any economic sanctions, whether imposed by the UN or by any country with which it does business or which otherwise applies to the company, its directors, officers and employees. ‘There must be appropriate due diligence in relation to third parties, transactions or activities that present a potential risk in relation to sanctions laws compliance,’ the policy declares.

However, in 2019, the company discovered that a shipload of fertiliser it had picked up in China destined for its customers in India had in fact been sourced in Iran. Fearful that it would breach sanctions in the US, where it derives a third of its revenue, Incitec Pivot swiftly offloaded the cargo at the nearest Chinese port.

The need for vigilance is even greater in financial institutions. The US authorities have focused on stopping money flowing to sanctioned nations, organisations and individuals. Banks have dealings with literally millions of customers and counterparties and can easily misstep.

Westpac has agreed to a fine of $1.3 billion over its failure to meet disciplines on international financial transfers imposed by the Financial Action Task Force (FATF), which is a multilateral body affiliated with the Organisation for Economic Co-operation and Development (OECD), setting standards for regulating money laundering and the financing of terrorism. Westpac had allowed offshore banks to use its domestic infrastructure to process Australian dollar payments in order to avoid transaction costs on international transfers.

Financial regulator AUSTRAC said the bank was dealing with high-risk institutions that were known to have relationships with sanctioned countries, including Iraq, Lebanon, Ukraine, Zimbabwe and the Democratic Republic of Congo:

The risk posed to Westpac was that these high risk or sanctioned countries may have been able to access the Australian payment system through these nested arrangements, unbeknownst to Westpac.13

The Trump administration has transformed the US approach to sanctions. Under the Obama administration, the US was adding an average of 520 entities a year to its sanctions list. Since Trump took office in 2017, the annual rate has doubled to an average of 1,070. The consolidated list of individuals and entities named under these sanction regimes is 1,380 pages long. Over the past 15 years, the number of separate US sanction regimes has risen from 17 to 30.
Severe penalties apply to a business found to have direct or indirect dealings with any of the targeted countries. A decade ago, fines averaged US$5 million a year, but by 2019 the US Treasury was collecting US$1.4 billion in fines for breaches.

Formal sanctions regimes are only one of several means of economic coercion. The US has long maintained a list of prohibited technology exports. The Trump administration is extending the list to a wide range of sales from US technology companies to Chinese businesses. Partly, this reflects a growing appreciation of the dual military and civilian use of some sensitive technologies and the growing vulnerability of critical infrastructure to cyber interventions. The US believes Chinese technology companies Huawei and ZTE pose national security risks and has for that reason imposed export controls on them.

However, the US is also using export controls as a coercive tool in its broader campaign on human rights. Chinese video surveillance company Hikvision was placed on the ‘entity list’ and barred from using US-derived technology, along with seven other Chinese artificial intelligence companies, over their involvement in the treatment of Uyghur people in the Xinjiang Uyghur Autonomous Region.

The US has also given consideration to barring Chinese access to US financial infrastructure, such as listings on US share markets.

There’s a large overlap between the targets of UN and US sanctions. Where the US doesn’t have UN support for sanctions regimes, it has sought to obtain broader backing. The US persuaded the Organization of American States to exclude Cuba and impose sanctions in 1962 and has recently won the support of Latin American nations to sanction Venezuela.

However, the US has always been prepared to pursue a unilateral path if it doesn’t obtain broader support. The Trump administration has intensified the use of sanctions against Iran, Cuba and Russia in the absence of widespread international backing. The US has also been prepared to take action against allies, recently imposing sanctions on any company working on a European–Russian pipeline project bringing gas from Siberia to Germany.

Washington has made a determined effort to force other countries to comply with its unilateral sanctions by presenting them with a choice: they can trade with the sanctioned nation or with the US, but not both. In 1996, under the Clinton administration, Congress passed legislation giving extraterritorial force to its sanctions on Cuba, Iran and Libya. People and businesses trading with those countries were forbidden from entering the US or trading with it.

The legislation affecting Cuba (the Helms–Burton Act) included a provision enabling US citizens to sue any foreign entity making use of assets expropriated from them by the Cuban Government following the 1959 revolution. The EU challenged the law before the newly formed WTO in 1996, claiming that the law’s extraterritorial reach broke WTO rules. The US argued that it was covered by the national security exemption, but it agreed to suspend the section of the law governing private legal actions, and the EU withdrew its WTO claim. The section has recently been implemented for the first time by the Trump administration, which has reversed the Obama administration’s relaxation of sanctions on Cuba.

Although the major US legislation, like the UN sanctions article, is structured around aggression and threats to national security, the US has developed law aimed specifically at abuses of human rights and corruption and targeting individuals.

The initial Magnitsky Act was passed by US Congress in 2012 to punish Russian officials involved in the torture and killing of a tax accountant, Sergei Magnitsky, who had been probing official corruption. It was expanded in 2016 to enable the US to impose sanctions on those it sees as human rights offenders, freezing their assets and banning them from entering the US. Unlike other US sanction regimes, it doesn’t require the President to declare a state of national emergency before imposition.
The Trump administration has sanctioned about 200 individuals under the legislation, ranging from corrupt Cambodian officials to a Latvian oligarch, a Serbian arms dealer, a Pakistani police superintendent and four senior Myanmar military officials. Canada and the UK have implemented similar legislation, and the EU is expected to follow suit. Australia is considering the case for similar action through a parliamentary inquiry that’s currently underway.

The US has made increasing use of its control over US dollar transactions to give extraterritorial force to its sanctions. In the wake of the 2001 terrorist attacks in the US, there was a concerted global effort to halt the financing of terrorist organisations. The OECD-affiliated FATF, which had been established in the 1980s to counter money laundering, was given a broader remit to stop money flows to terrorists, while the Bush administration gave the US Treasury the power to order US banks to withhold services from any sanctioned entity, individual or ‘money laundering concern’.

Fear of falling foul of those provisions has helped make US sanctions on Iran, Venezuela, Cuba and North Korea, among others, effective internationally. When Russian company Rusal (the world’s second largest aluminium producer) was sanctioned in 2018 in response to allegations of Russian meddling in the 2016 US presidential election, its customers were given 30 days to conclude transactions or face being locked out of the US financial system. The disruption was so great, sending aluminium prices soaring, that the US Treasury provided exemptions and ultimately withdrew the sanctions after the Russian oligarch who owned the business agreed to relinquish control.

The US isn’t alone in using financial sanctions. The EU sought to persuade Iran to negotiate over its nuclear program in 2012 by ordering the agency that completes international financial transactions to expel sanctioned Iranian banks. The Belgium-based Society for Worldwide Interbank Financial Telecommunications (SWIFT) is an international cooperative of financial institutions and is the indispensable communications infrastructure for the global financial system.

Iranian banks were allowed to return after a nuclear deal was struck in 2015. When the Trump administration pushed for them to be expelled again after Trump unilaterally withdrew from the nuclear agreement, the EU objected. SWIFT is covered by Belgian law but complied with the US, arguing that global financial stability would be endangered if it became the target of US sanctions.

Both China and Russia have built their own payments communications infrastructure to ease the threat of US sanctions, but the US dollar’s role as the dominant global currency is likely to continue. It gives the US a power to impose its foreign policy towards targeted nations on third countries, which may pursue quite divergent policy.

The US must be wary of overplaying its hand. The head of the US Treasury’s financial crimes and terrorist financing division under the George W Bush administration, Juan Zarate, recounts that in 2003 US officials proposed cyberattacks on Iraqi assets by penetrating bank computers around the world covertly and setting Iraqi account balances to zero. Treasury officials successfully argued that the plan would shatter confidence and outrage allies.

More recently, the Treasury has had to push back against suggestions that the US should cancel China’s US$1 trillion investment in US Government bonds, which has been advocated by Republican members of Congress. Such a move would destroy global confidence in the US bond market.
The effectiveness of economic coercion depends on both the target’s response and the coercer’s ability to hit the target.

Responding to veiled threats

Fear of the consequences of displeasing China has enabled its authorities to hold the line on a series of issues that are important to it and to shift the behaviour of companies and countries in ways that align with its interests. Airlines and international hotel chains don’t refer to Taiwan as a separate state, world leaders don’t meet the Dalai Lama, and the Muslim world has remained largely silent about the incarceration of millions of its co-religionists in Xinjiang.

But when issues of importance to the target of its coercion are at stake, the outcome is less certain, as China’s threats can strengthen the resolve of the target government.

Canada would doubtless have much preferred that the US hadn’t made an extradition request for Huawei’s finance director, but, when that happened, the Canadian Government wasn’t going to interfere in the legal process in the face of Chinese coercion. ‘Canada has an independent judiciary and those processes will unfold independently of any political pressure, including by foreign governments,’ Prime Minister Justin Trudeau said, adding that to give in to intimidation would simply make Canadians around the world more vulnerable. Beijing’s coercion has demonstrated the risks to Canada in its relationship with China and led to a deterioration in public sentiment as well as a hardening of public policy.

In a similar vein, Australia’s Prime Minister Scott Morrison responded to Chinese threats to tourism and education, telling a radio interviewer, ‘We are an open trading nation, mate, but I’m never going to trade my values in response to coercion from wherever it comes.’

China’s most concerted coercive campaign was against South Korea after Seoul’s decision to allow the US to deploy an anti-missile system on its territory to protect South Korea from North Korean missiles. After a year of boycotts of Korean goods and tourism and harassment of the Lotte supermarket chain in China, the South Korean Government negotiated a military deal to ‘normalise’ relations. That included commitments that South Korea wouldn’t add further to the missile defence system installed by the US, wouldn’t participate in a broader US missile defence network and wouldn’t join a trilateral military alliance with the US and Japan.

It’s hard to determine how much of a victory that was for China. It didn’t halt the installation of the missile defence system being built by the US. South Korea had no plans to add to it or to join any broader US missile defence system across the North Asia region. In South Korea, which has a history of considerable hostility towards Japan, there was no appetite for the trilateral alliance ruled out in the agreement with China. However, the South Korean Government did negotiate to limit its future military options, however remote, under the pressure of Chinese coercion. And the economic pain suffered may have made South Korean authorities doubly wary of offending the country’s major trading partner. From China’s perspective, the economic retribution may have achieved its goal.
A clearer example of Chinese coercion proving counterproductive is its threat to supplies of rare earth minerals. China’s pressure has resulted in its exclusion from any new rare-earth developments in Australia and the promotion of alternative supplies by Japan and, potentially, the US and Australia.

While most of China’s economic coercion involves curbing access to its markets, it has long seen its near monopoly of the production of rare earths and downstream products as giving it a resource weapon, akin to the influence on the oil market wielded by the Organization of the Petroleum Exporting Countries. China accounts for around 80% of global rare-earth production and up to 100% of the market for many specialised rare-earth products.

In 2010, at the peak of a dispute over the sovereignty of uninhabited islands claimed by both China and Japan, China reacted to the arrest of a Chinese fishing vessel by suspending rare-earth shipments to Japan. Japan had developed world-leading technology for rare-earth permanent magnets and had built a thriving industry on the strength of applications for rare earths and other critical minerals. China was the source of almost all its raw materials.

The suspension of shipments was, typically, denied by China. Its premier at the time, Wen Jiabao, declared: ‘We haven’t imposed, and will not impose, an embargo on the [rare-earths] industry.’

However, Japan’s government set aside US$1.25 billion to mitigate future disruptions, funding research into rare-earth substitutes and developing non-Chinese supplies. The development of Australia’s Lynas Corporation, which is now the biggest non-Chinese rare-earths supplier, was financed by the Japanese Government. China’s share of the Japanese market is now a little over half.

The US remains heavily dependent on Chinese rare-earth supplies, which were threatened in 2019 following the US decision to bar the sale of technology to Chinese telecommunications firms Huawei and ZTE.

China’s National Development and Reform Commission released a bulletin quoting an unnamed official in a scripted Q&A:

Will rare earths become China’s counter-weapon against the US’s unwarranted suppression? What I can tell you is that if anyone wants to use products made from rare earth to curb the development of China, then the people of the revolutionary soviet base and the whole Chinese people will not be happy.18

In other words, if the US was going to ban the export to China of technology that used Chinese rare-earth products, then the US couldn’t expect China to continue supplying those products.

The Chinese Government didn’t follow through with the threatened boycott, but the Australian Government appears to have made a decision to prohibit any further Chinese investment in Australia’s critical minerals industry. Defence Minister Linda Reynolds set out the government’s concern late last year, telling a conference on new metals that ‘The key vulnerability to this industry is the dominance of a single nation across the production and supply chains. That is our critical vulnerability—a single nation dominates that supply chain.’19

Chinese investors have been active participants in the Australian critical minerals sector, which is heavily populated by development companies with resources needing to be proven, buyer contracts secured and project finance arranged. Chinese businesses have been stakeholders in a number of development companies, including Northern Minerals, Arafura Resources and Greenland Minerals.

In two significant decisions in April this year, the Treasurer rejected Chinese investment proposals for two critical minerals projects. Both were for stakes of no more than 12% in development companies. The principal asset of one of them wasn’t even in Australia but in the Republic of the Congo, with elevated political risk.

Vetoes of foreign acquisitions by Australia’s Foreign Investment Review Board are rare, and the rejection of such small stakes is without precedent. If such minor investments aren’t acceptable, the implication is that no further Chinese participation in the Australian critical minerals industry will be permitted in the light of China’s threats to use its dominant market position as leverage in its economic disputes with the US. China’s threats strengthened the resolve of its intended target.
Hitting the target

George W Bush pulled off a diplomatic triumph in December 2006, persuading Russia's Vladimir Putin and China's Hu Jintao to support a US-led push for the UN to impose sanctions on Iran over its nuclear program. A month earlier, Russia's Foreign Minister, Sergey Lavrov, and China’s UN Ambassador, Wang Guangya, had both publicly rejected the use of sanctions. Lavrov said that Russia couldn’t support measures aimed at ‘isolating Iran from the outside world’, while Wang argued that Iran's nuclear program had a peaceful intent.20

However, following personal calls from Bush to the Russian and Chinese leaders, a unanimous UN Security Council resolution banned arms sales and shipments of materials and technology relevant to Iran's nuclear program. While Iran's President, Mahmoud Ahmadinejad, brushed off the UN sanctions as akin to 'annoying flies, like used tissue', Bush and his successor, Barack Obama, were able to retain UN Security Council support for successively tighter sanctions.21

Russia and China had their separate reasons for going along with the US. Russia didn't want to see an arms race on its southern border. China was working cooperatively with the US on North Korea and didn't want to upset its trade relationship, which was flourishing in the wake of its accession to the WTO.

In theory, there's an inflection point at which the pain caused by sanctions balances the resolve of the target nation to persist with the behaviour that’s causing offence, and a deal can be struck. While the level of pain can be calibrated, the resolve of the target is harder to predict.

In Iran's case, the inflection point was the surprise victory of the relatively moderate Hassan Rouhani at the 2013 presidential elections on promises to end the impasse over nuclear weapons, re-establish relations with the West and end the crippling sanctions that were choking the Iranian economy. Two years later, Iran struck a deal with the five permanent members of the UN Security Council (the US, Russia, China, France and the UK) as well as Germany to wind back its nuclear program.

The deal never went far enough for many critics but showed that economic coercion could work. Without the pain of sanctions, Iran wouldn't have been brought to the negotiating table.

The Iranian experience since the Trump administration withdrew from the nuclear deal in 2018 and redoubled the force of unilateral US sanctions shows the fickle nature of national resolve. The increased sanctions are causing obvious hardship (the International Monetary Fund reported that Iran’s economy contracted by almost 10% in 2019). Sanctions have led directly to instability and widespread rioting in the wake of a 50% lift in petrol prices in November 2019.

However, at parliamentary elections in March this year, as the coronavirus was beginning to ravage the country, conservatives achieved a large majority, reducing the supporters of Rouhani to a small rump. The conservatives, who oppose deals with the West, are now favoured to win next year’s presidential election. Iranian officials are rallying domestic support, claiming that the refusal of the US to relax sanctions on shipments of medical equipment during the coronavirus pandemic is a ‘crime against humanity’.22

As one academic analyst of sanctions comments, the resolve of a target country should never be taken as a given but is ‘a factor that evolves as the sanctions effort unfolds, often in response to its pressure’.23

A widely quoted academic study examined all instances of economic sanctions between 1914 and 1990 and found that a third were successful (the study was later updated to 2000, with the same finding).24 A critique of the study concluded that almost half the cases chalked up as successes were in fact resolved by military force and claimed that the real success rate was just 5%.25
While six decades of economic sanctions have failed to change the government of Cuba, it’s often difficult to gauge their impact. Sanctions may have contributed to the end of white rule in Rhodesia in 1979, but so too, surely, did the successes of its opponents in a guerrilla war. Sanctions might not have persuaded Russian proxies to abandon their guerrilla campaign in the Donbass region of Ukraine, but they may have led Russia to abandon plans to annex it. Sanctions encouraged the military rulers of Myanmar to embark on a process of democratisation in 2012, but they didn’t stop the persecution of the Rohingya minority, and the military retains a major political role.

The intensification in the use of sanctions by the Trump administration has been accompanied by ever more ambitious objectives. It has said that it won’t relax sanctions on Cuba before Havana moves towards freedom and democracy, while sanctions on Venezuela aim for nothing less than regime change. Secretary of State Mike Pompeo set 12 conditions for Iran. As well as halting all nuclear enrichment in perpetuity, it was to halt all support for allied organisations Hezbollah and Hamas and for Houthi rebels in Yemen, disarm Shia militias in Iraq, withdraw all its forces from Syria and halt threats against Israel and Saudi Arabia.

One consequence of the redoubling of sanctions on Iran and Cuba after deals to relax them had been struck is the erosion of trust that target countries may have that any future deals would be honoured. Trump’s former national security adviser, Robert Bolton, cited the precedent of Libya when preparing for negotiations to persuade North Korea to abandon its nuclear program. Libya’s Muammar Gadaffi had abandoned his nuclear and chemical warfare programs in 2003–04 in order to gain relief from Western-led sanctions. As the New York Times, among others, pointed out, by 2011, Gadaffi had been overthrown in a NATO-backed campaign before being assassinated by rebels, so North Korea was never likely to find the example inspirational.26
The increasing resort to economic coercion is occurring as international economic relations generally have become more fractious.

The open embrace of globalisation from the mid-1980s through to the global financial crisis in 2007–08 has given way to a new economic nationalism. That’s most obviously true of the US and China, but is evident more broadly.

An ongoing survey of protectionism among G20 members counted 2,733 new trade-distorting measures, such as tariffs, duties and quotas, between 2017 and 2019, only 23% of which involved the US or China. The WTO no longer has the ability to adjudicate disputes, as its appeals tribunal has been left without a quorum of judges because of a US veto on all new appointments.

As the rules governing global commerce lose their force, it becomes easier for disputes to be mediated by the exercise of economic power.

The rise in economic coercion is a new reality that Australian policymakers and businesses must acknowledge. Businesses with international exposure are more likely to find themselves dealing with counterparties that also have connections with sanctioned entities and individuals. There’s a growing level of political risk in some of the markets that Australian businesses serve.

With the growing politicisation of trade, there’s a case for the federal government to include the Trade Minister in the National Security Committee of Cabinet to ensure both that they embark on any trade negotiations fully aware of national security priorities and that the direction of national security policy is decided in full awareness of the economic and trade consequences. The Trade Minister has direct engagement with the trade authorities of other nations and an understanding of the politics of trade that it can’t be assumed will be shared by the Foreign Minister.

In the case of China, companies need to factor into their strategic thinking the possibility of markets being closed for political reasons and their individual businesses facing risks to their activities, not just sales and trade but also the arbitrary detention of employees. Political risk assessments should be an essential component of board planning. The pretext for potential boycotts can’t be predicted, and business should be aware that the Australian Government is most unlikely to shift policy under the pressure of coercion.

The big resource companies selling raw materials that are essential to China’s industrial development are relatively secure, but sectors such as education and tourism are exposed. Some universities made a strategic decision to increase the proportion of their staff on limited-term contracts to increase their flexibility to deal with a sudden drop in international student numbers, but the closure of borders in response to the Covid-19 pandemic has nevertheless exposed the financial vulnerability of their business model. Farm groups are similarly vulnerable, as the tariffs imposed on barley and health certification restrictions on Australian beef have shown.

Business groups affected by Chinese coercive measures imposed because of governments’ political conflicts may seek government compensation. In the US, compensation was arranged for farm groups affected by the tariff war with China, while the South Korean Government offered compensation to tourism companies affected by the loss of Chinese business during its dispute.
Businesses can insure for sovereign risk, but the government always has the right to act in the international sphere as it sees fit. Governments can’t be expected to compensate for what’s, essentially, sovereign risk. However, a government could decide to offer structural adjustment assistance to sectors to help them to diversify their markets. That could be a demonstration of its resolve.

Both governments and business organisations should stand ready to call out attempted coercion of individual companies and should provide representative support and guidance.

Any government that becomes the target of economic coercion can expect to come under pressure from business lobbies and other interest groups to placate the coercive nation. In Australia, there have been calls from entrepreneurs who have profited from China’s appetite for Australian resources for the government to take the initiative in smoothing the bilateral relationship. The Canadian Government has seen similar calls from business leaders, urging that extradition proceedings against the Huawei finance director be halted. The experience of the targets of coercion from both China and the US is that it takes political resolve to resist those pressures.

In the case of sanctions, Australian companies with international operations at risk of becoming collateral damage from economic coercion need to implement sanctions compliance programs. The US Office of Foreign Assets Control provides comprehensive guidance on the ingredients of an effective sanctions compliance program. They include management commitment, vesting a compliance unit with the resources and authority to enforce it, and having a formal process of risk assessment involving the close vetting of new customers, suppliers and acquired businesses.

Australia should take its sanctions regulation more seriously by transferring responsibility for that regulation from the Department of Foreign Affairs and Trade (DFAT) to AUSTRAC. DFAT doesn’t have the regulatory culture needed to sharpen businesses’ awareness of the risks they confront. AUSTRAC’s Commonwealth Bank and Westpac prosecutions show that it understands the strictures that govern international finance and the standards that international companies have to meet.

Australia was a key participant in the formation of the WTO in 1995 and has prospered under the WTO’s rules-based framework promoting free trade. The development of a more conflicted global economic environment, with the exercise of economic coercion as its ultimate expression, is damaging to our national interests. International forums, such as the G20, the Asia–Pacific Economic Cooperation forum, the OECD and the WTO, should be concerned about the growing use of economic coercion, which is a threat to the freedom of commerce.

The WTO has been used in the past to push back against economic coercion. Europe persuaded the US to suspend the implementation of key elements of the Helms–Burton Act that extended the extraterritorial reach of its sanctions, by taking action against it at the WTO, while Japan and the US successfully fought a WTO case to force China to abandon its export controls on rare earths.

The Australian Government has canvassed taking China’s application of tariffs on barley to the WTO and should do so. It should explore the potential for joint approaches with Canada and other nations affected by coercion. China prefers to deal bilaterally because that maximises its power, so any opportunity to use multilateral forums should be seized.

The Australian Government should oppose the widening use of the WTO’s national security exemptions from the normal rules of free trade. It should also be ready to oppose the imposition of US sanctions where it believes they cut across Australia’s national interest.

Australia’s strong national interest is the preservation of the world trading system governed by clear and universally accepted rules with a respected means of adjudicating disputes. The system isn’t set in stone—it can absorb change and reform—but it can also be undermined, particularly if it loses the respect of major powers. The growing use of economic coercion by major powers is a threat to the free flow of trade and investment that’s fundamental both to global prosperity and to the wellbeing of smaller and mid-sized nations lacking in unilateral clout. The Australian Government should strongly endorse the WTO and the rules-based framework that the WTO administers.
Australia’s regulation of sanctions

Australia splits the regulation of sanctions, which is administered by a section of the legal department of DFAT, and the regulation of money laundering and the financing of terrorism, which is administered by AUSTRAC, which is under the Department of Home Affairs. Australia’s consolidated list of sanctions includes almost 6,000 entries, and the government imposes its own sanctions without UN endorsement on Myanmar, Russia, Syria and Zimbabwe.

The FATF believes that Australia doesn’t take the regulation of sanctions sufficiently seriously. In 2014, the agency’s review of the Australian regulatory structure concluded that:

- DFAT does not adequately monitor or supervise the financial sector for compliance with the requirements of the FATF Recommendations, as would be expected of a supervisory authority. In addition, no financial institutions are supervised or monitored for compliance with the targeted financial sanctions requirements (as in financial supervision) by any other competent supervisory authority.29

The FATF has been complimentary about the efficiency with which Australia lists the targets of our financial sanctions and is satisfied with the severity of the penalties. However, it says that the effectiveness of our sanctions framework is compromised by ‘the lack of financial supervision of the financial and designated non-financial business and professions sectors to ensure compliance’.

While Australian governments have worked to address many of the FATF’s concerns about the country’s vigilance over the financing of terrorism and money laundering, the essential structure of the regulation of sanctions is unchanged.

Through 2019, there was discussion about shifting responsibility for sanctions regulation to AUSTRAC so that there would be a single regulator. Despite having few regulatory functions beyond the issuing of passports, DFAT has held on and formally named its legal department section the ‘Australian Sanctions Office’ on 1 January 2020.

By its own admission, it’s a weak regulator with only seven staff. In a formal self-assessment in 2019, it acknowledged that:

- Unlike some Australian Government regulators which have a broader mandate to undertake compliance and monitoring, [the sanctions section] has a limited role in enforcing and monitoring compliance with Australian sanctions law.30

Instead, it relies on the Australian Federal Police and the Australian Border Force to investigate any noncompliance that the section identifies. In practice, there have been only two prosecutions in Australia. An Iranian man has been prosecuted over allegations that he shipped 90 tonnes of nickel alloy to Dubai, knowing it was destined for Iran. The second case concerns a South Korean-born Australian citizen alleged to have planned the sale of coal and missile parts to North Korea.

Australian corporations and other entities are unlikely to take compliance with sanctions seriously in the absence of a serious regulator. For Australian entities with international engagement, the regulator of greatest concern is the US Office of Foreign Assets Control.

If one of the Australia’s big four banks has been paying inadequate attention to the management controls required to comply with international sanction law, along with money laundering and terrorism finance, it’s likely that smaller financial institutions are also exposed. Although they may believe they’re safe from the reach of US regulators because their business is almost wholly domestic, they’re likely to have clients and correspondent banking relationships with international exposure. They’re also likely to have exposure to US dollar transactions.

Non-financial corporations are also at risk. The US Bureau of Economic Analysis identifies 1,100 Australian businesses with subsidiaries or branches in the US with sales or assets of more than US$25 million.31
The dependence of universities on a flow of international students and research creates special vulnerabilities. Most Australian universities have sanctions policies to guide compliance with Australian and UN sanctions. While they can accept students from sanctioned nations, those students’ research topics must be approved to ensure that they have no relevance to military or weapons capabilities. Any change in research topic must be vetted for security implications. Payment for tuition by any third party must be cleared to ensure that they aren’t on Australia’s sanctions list. Universities may also be exposed through academic visits and conferences held in sanctioned nations, research collaborations and the employment of academics.
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