Understanding sanctions with the Global Sanctions Index (GSI)

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LSEG RISK INTELLIGENCE

Executive summary

- In April 2022 the Global Sanctions Index (GSI) stood at 255 and year-on-year inflation was **10.7%** with over 47,000 persons (individuals and entities) sanctioned
- Since January 2017, sanctions have **increased by 255%**
- Recent sanctions on Russia have been unprecedented in many ways – the targets of the sanctions include some of Russia's biggest companies and richest people, as well as senior politicians and the central bank. The volume of sanctions update activity was immense (over 15,000 updates in March and over 9,000 in April), but the **total number of deduplicated sanctions** nevertheless grew at a modest pace. **The volume of new sanctions does not have to be at an unprecedented level for the consequences to be unprecedented**
- Sanctions inflation costs are high – both to society and to institutions directly
- Institutions should carefully design their screening programmes to adapt to the rapidly growing number and complexity of sanctions regimes

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Introduction

Economic sanctions have rapidly increased in popularity, number and complexity over the last decade. Long a part of interstate relations, sanctions have been used since as early as the Megarian Decree in 432 BCE, when Megarian traders were banned from Athenian marketplaces – one of the first recorded examples of economic sanctions used as a foreign policy tool. Short of war, sanctions have subsequently become the preeminent tool for interstate coercion. As the Russian invasion of Ukraine reminds us, states use sanctions as the primary tool to deter, punish or condemn certain actions by other countries or persons beyond the reach of their law enforcement authorities.

Whilst the increase in sanctions is obvious, it is difficult to quantify them in detail or track them globally over time. To do so would require regular and timely monitoring of all relevant sanctions lists issued anywhere, then critically deduplicating these lists. LSEG's World-Check database has quantified and tracked sanctions lists for 22 years, offering reliable data to our customers worldwide. In a world awash with frequent changes to inflation, economic growth, retail sales and unemployment rates time-series data, access to comparable sanctions data is critically important.

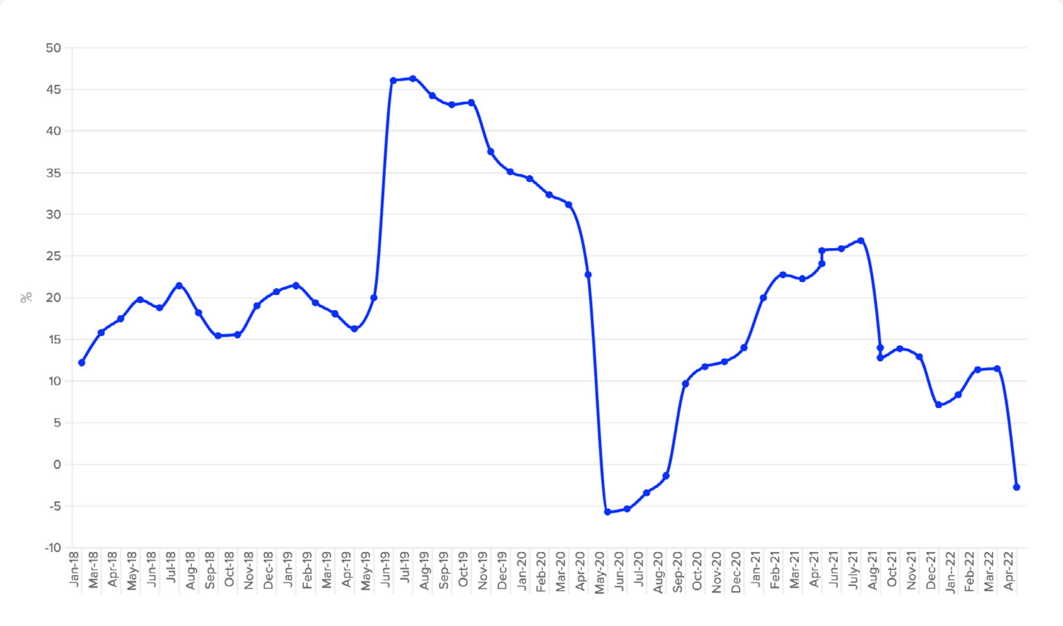
At LSEG, we are launching the Global Sanctions Index (GSI), based on deduplicated data from World-Check, that covers the net increase in explicit sanctions on natural and legal persons from every known, publicly available sanctions list globally. The index base date (when it equalled 100) is January 2017 and it is equally weighted across all countries and sanctions programmes. For more details on how the index is constructed, please refer to the Global Sanctions Index methodology section at the end of this paper.

Key findings

In April 2022 the GSI stood at 255 and year-on-year inflation was **10.7%** with over 47,000 persons sanctioned, representing a dramatic slowdown from a year earlier when sanctions inflation stood at 24.7% (index = 227). This reduction in sanctions inflation was recorded despite the unprecedented sanctions that have been imposed on Russia during the first few months of 2022 – which indicates **these sanctions are severe in consequence but are not unprecedented from a volume perspective.** According to World-Check data, in absolute net terms, over 1,600 persons have been added to sanctions lists in 2022, ranking it 17th out of a total of 60 three-month periods since 2017.

Since the June 2021 spike in sanctions inflation, it has steadily declined (see chart below), following a small deflationary period in mid-2020 after sanctions hyperinflation that was driven by terrorist-related designations by Pakistan and other countries in 2019.

Global sanctions inflation data (January 2018 to April 2022)

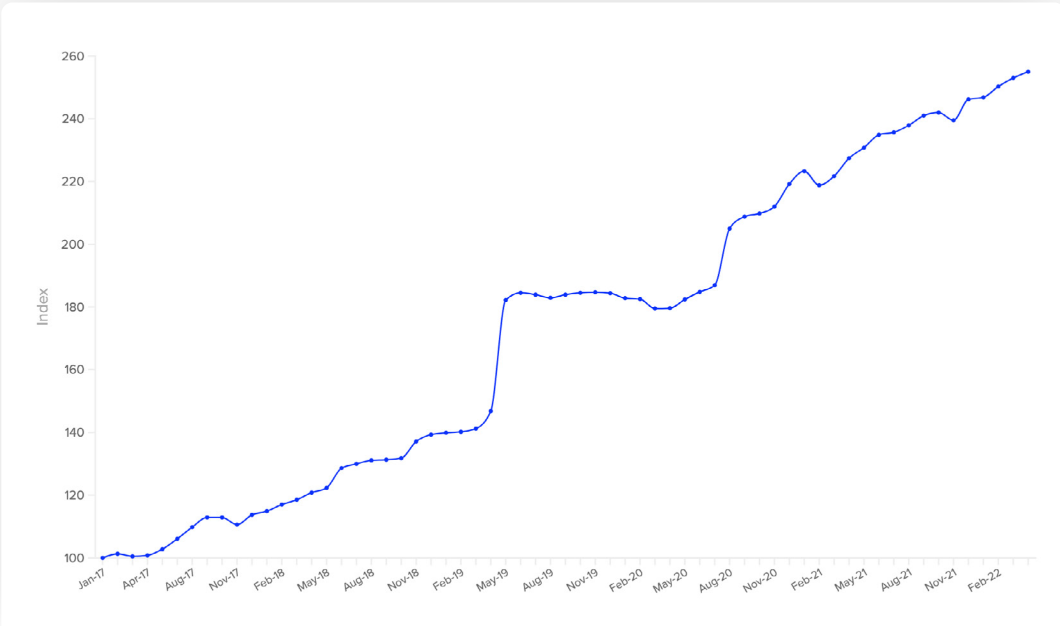


Source: World-Check data

[redacted]

Over the period from January 2017, explicitly sanctioned persons on a deduplicated basis increased by **255%,** from just over 18,500 sanctioned persons to over 47,000 in April 2022 (see chart below).

Explicitly sanctioned persons on a deduplicated basis (January 2017 to April 2022)



Source: World-Check data

Although the data shown in these two charts is significant, it underplays the practical challenges related to sanctions. Sanctioning bodies do not simply announce one name for each sanctioned individual, but they often announce multiple and sometimes dozens of names. This multiplier effect adds many more names to the sanctions list: the 47,000 sanctioned individuals mentioned above have over 190,000 additional aliases (excluding low-quality aliases).

Comparing this to the size of William Shakespeare's Complete Works, a volume which contains 5.3 million characters (without spaces) in over 1,200 pages, the combined names and alias fields of all sanctioned persons globally – again excluding low-quality aliases – contains over 5.6 million characters (again without spaces).

Sanctions activities versus net sanctions growth

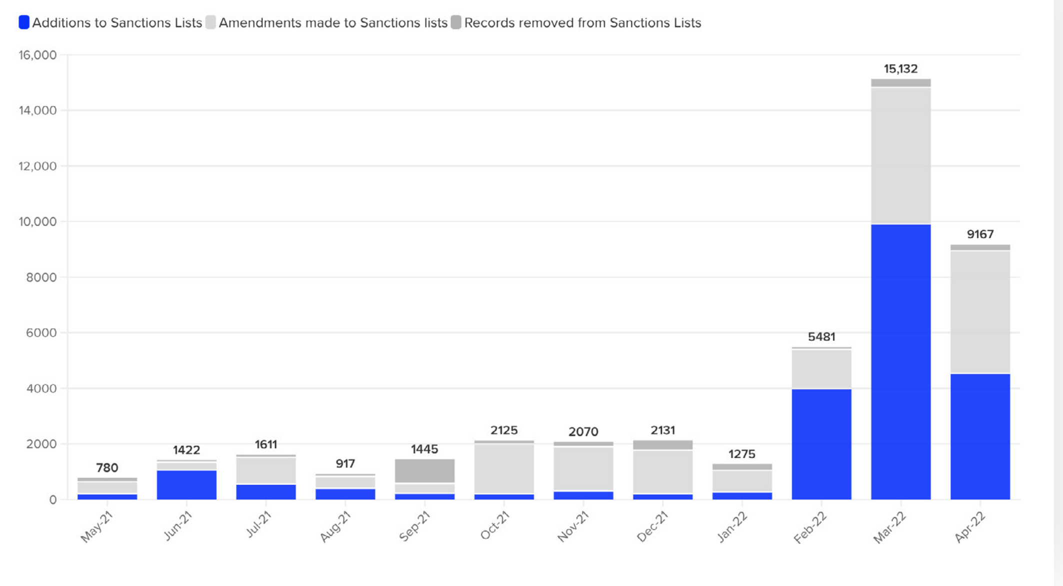
Due to the unprecedented sanctions imposed by numerous countries on Russia, February and March 2022 were busy times for many sanctions teams – and still, sanctions inflation was just 10.7% annually and 1% monthly in March.

How could this be possible?

There were waves of sanctions activities by different bodies (the US, EU, UK, Japan, Singapore, Australia amongst others) targeting a small number of unique persons, but the updates happened at different times. As an example, the European Union sanctioned 351 members of the Russian State Duma on 23 February, and the Office of Foreign Assets Control (OFAC) followed suit on 24 March. On a deduplicated basis, OFAC's actions did not add to sanctions inflation, but still represented sanctions activity that compliance teams would respond to.

This is seen as we graph sanctions activities on a 'not duplicated' basis:

Not deduplicated sanctions additions and changes. Explicit sanctions activity



Exploring the consequences of sanctions inflation

Price inflation is one of the most closely watched economic metrics: the media, consumers, policymakers, central banks, investors all track it closely. The reason for this is obvious: deflation or high inflation can have devastating economic effects, introducing wide-ranging consequences for consumer behaviour, interest rates, rates of return and other economic factors.

Whilst sanctions inflation has clear consequences beyond price inflation, it can have a substantial impact on the compliance profession directly, as well as on consumers and entire supply chains.

The most obvious consequence of more sanctioned persons is more risk, because every additional person added to a sanctions list increases the possibility of falling afoul of sanctions regulation. This risk varies by the sanctions issuing body, how seriously they take enforcement and the exact detail of the sanctions imposed.

However, there are less obvious consequences of sanctions inflation. More names (especially more new names) **drive up screening match rates and thus the cost of compliance.** Explicit sanctions are routinely screened in a group against all customer and at least cross-border transactions. Matches are good when true positives are identified and the risks associated with them mitigated (e.g., blocking or allowing a transaction involving a sanctioned person), but typically match rates are dominated by **false positives**.

In a well-designed screening programme, false positives can typically only be identified as such ex-post, that is, after a human or analyst has adjudicated it. It is typically only possible to say with a reasonable degree of confidence that a potential match is a false positive after a human review. Increased false positive rates drive up operational costs for several reasons: more analysts are needed to review more matches, which requires training, IT and HR resources, licenses from vendors, office space and other resources. Moreover, false positives can interfere with legitimate business and impose indirect costs, including blocking transactions, even if temporarily, or requiring slow and expensive Know Your Customer (KYC) remediation exercises in order to confirm if a customer is sanctioned or not.

When risks are high, institutions may decide to avoid certain types of business entirely. Whilst the process of derisking may be attractive for individual financial institutions, the economic consequences to society as a whole can be very negative. In particular, derisking can disproportionally impact vulnerable people and countries, leading to financial exclusion.

Finally, as sanctions regimes have become more complex, deciding what to do with true matches has become far more complicated, often requiring senior compliance staff, in-house or external counsel and sanctions experts to become directly involved. Very different rules apply to sanctioned persons depending on the country imposing the sanctions and the exact programme in question, both of which can require significant expert involvement. Also, as more countries have issued autonomous sanctions, often in direct contradiction to each other – such as Ukraine on Russia and Russia on Ukraine, the US on China, and China on the US – more conflicts of laws arise that put institutions in an impossible situation.

In short, there are significant costs for institutions, but also to society. As the cost of compliance increases, this indirectly raises the costs of financial services, leading to more derisking and complexity.

Conclusion

Sanctions inflation has been significant over the last five years, more than doubling in number whilst also becoming inherently much more complex. Although the consequences of sanctions inflation have not been widely discussed, they need to be. The costs to institutions and to society are substantial, and make a well-designed screening programme with good matching and reliable data absolutely critical.

Considerations for institutions

As the number and complexity of sanctions regimes have proliferated, the importance of having a formal design mindset to screening has become even more important. In light of this, institutions may decide to:

– **Identify and screen only relevant lists.** Data vendors, including World-Check, scrutinise all sanctions regimes because they serve customers in all markets, but typically only lists in specific jurisdictions will be relevant to any given institution

– **Adopt a 'default-zero' approach that is incremental.** Start with no sanctions lists then include any lists that are considered to be relevant. Avoid starting with all lists then finding reasons to exclude a list

– Use **first-rate fuzzy matching technology** and set a matching threshold that matches the institution's risk appetite

– Use **high-quality data** enriched with secondary identifiers that allows maximum automated adjudication for possible matches (e.g., using dates of birth to dismiss possible matches).

Global Sanctions Index (GSI) methodology

The Global Sanctions Index (GSI) takes its base as January 2017 (=100) and includes every explicit sanctions regime tracked by LSEG World-Check Risk Intelligence data, covering all keywords with the 'sanctions' keyword type. This means that implicit sanctions, for example, sanctions created by the OFAC 50% rule, are entirely excluded from this analysis.

The sanctions regimes tracked are very broad, ranging from consensus-driven United Nations (UN) sanctions that are typically on the grounds of terrorism, to autonomous sanctions issued by nation states such as the US, Pakistan, Australia, Switzerland, Japan and Ukraine, to those issued by regional bodies such as the European Union. The reasons for designation vary as well, across alleged involvement in terrorism or the financing of terrorism, designations for narcotics trafficking (like the Kingpin Act designations), proliferation, human rights abuses, corruption, alleged involvement in election interference, sanctions imposed on Russia for the invasion of Ukraine, amongst others.

The consequences or severity of the sanctions are not considered. However, we have included various considerations, from blocking orders to travel bans to purely investment bans. Similarly, all sanctions targets have been included for natural persons, companies, trusts, vessels and aircraft.

Note that in any given month, individuals or entities can be added and deleted from sanctions lists, so the GSI will track only the net number.

About the Author

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Mike leads LSEG's Customer & Third-Party Risk Solutions business in Asia. In this role, he helps define LSEG's go-to-market, product and content strategies, including for the flagship World-Check, Qual-ID and LSEG Due Diligence products. He is particularly focused on keeping abreast of regulatory, industry and technological developments to ensure LSEG continues to innovate and develop products that meet client needs.

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