



Observatoire ARGA

**SANCTIONS AND COMPLIANCE ASYMMETRY UNDER CONDITIONS OF
GEOPOLITICAL TURBULENCE: A STRUCTURAL ASSESSMENT OF RISKS TO
ASIA'S INVESTMENT NEUTRALITY**

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Purpose of the Document:

To analyze the impact of global geopolitical turbulence and sanctions asymmetry on the investment neutrality and financial stability of Asian financial centers, and to propose institutional mechanisms for balancing associated risks.

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1. EXECUTIVE SUMMARY

Asian financial centers have traditionally positioned themselves as neutral, predictable, and institutionally stable platforms for global capital allocation. Their competitive advantage is grounded in transparent regulation, judicial independence, and openness to cross-border financial flows.

Amid rising geopolitical tensions and the expansion of sanctions regimes, the risk of sanctions and compliance asymmetry has intensified. Sanctions asymmetry arises when restrictive measures formulated outside the region generate indirect pressure on banks and investment structures in Asia, even where the relevant jurisdiction has not formally adopted such measures.

This pressure manifests through defensive compliance, contraction of correspondent and investment relationships, revision of fund strategies, and increased compliance burdens. The key challenge lies in preserving investment neutrality while simultaneously adhering to international AML/CFT and sanctions compliance standards.

This report proposes a structural framework for analyzing sanctions asymmetry, assessing its systemic implications, and identifying risk-balancing mechanisms to support the resilience of Asia's financial centers.

2. GEOPOLITICAL TURBULENCE AND GLOBAL SANCTIONS DYNAMICS

2.1. Expansion of Sanctions Regimes

Sanctions are increasingly deployed as instruments of foreign policy and economic leverage. There has been a marked growth in sanctions lists, expansion of sectoral restrictions, and intensification of secondary sanctions.

2.2. Extraterritorial Effects

Even in the absence of formal participation in a sanctions regime, banks must account for global risks associated with U.S. dollar infrastructure, correspondent banking relationships, and cross-border settlement systems. Extraterritorial effects create de facto regulatory influence through market mechanisms.

2.3. Pressure on Neutral Jurisdictions

Financial centers seeking to preserve neutrality face indirect pressure from international partners, rating agencies, and global investors. Such dynamics may constrain the scope for independent regulatory positioning and policy flexibility.

3. THE CONCEPT OF INVESTMENT NEUTRALITY

Investment neutrality implies:

- equal and non-discriminatory treatment of investors;
- predictability of regulation and law enforcement;
- absence of politicized pressure in decision-making;
- transparency in capital admission and servicing procedures;
- availability of effective appeal mechanisms.

Neutrality does not preclude adherence to international standards but requires proportionality, legal certainty, and consistency in application.

4. SANCTIONS ASYMMETRY AND COMPLIANCE BURDEN

4.1. Compliance Burden

Banks are compelled to consider external sanctions regimes even when such regimes are not legally binding at the national level. This results in expanded screening procedures, enhanced due diligence, and increased transaction monitoring costs.

4.2. Defensive Compliance

Under conditions of uncertainty, financial institutions may adopt stricter internal control standards to minimize regulatory and reputational risks. This may lead to excessive transaction refusals, client exits, and conservative risk classification practices.

4.3. Reputational Risks

Association with sanctions-sensitive entities may result in service denial, transaction freezes, or deterioration of financing terms, even in the absence of a direct legal violation. Reputational considerations thus amplify the practical impact of sanctions asymmetry.

5. PRESSURE FROM CORRESPONDENT AND INTERNATIONAL PARTNERS

5.1. Correspondent Relationships

Dependence on global payment infrastructure and correspondent banking networks increases sensitivity to sanctions-related signals. The risk of termination or restriction of correspondent relationships may incentivize excessively conservative compliance practices and precautionary disengagement from higher-risk clients or sectors.

Such structural dependence amplifies indirect sanctions exposure, even in jurisdictions that maintain formal neutrality.

5.2. International Funds

Global investors and investment funds may avoid jurisdictions perceived as carrying elevated sanctions risk, adjusting portfolio allocations and geographic exposure accordingly. This behavior affects market liquidity, depth of capital markets, and long-term investment stability.

Perceived regulatory uncertainty can therefore influence capital allocation decisions independently of formal legal obligations.

6. IMPACT ON CROSS-BORDER CAPITAL AND FUNDS

6.1. Capital Reallocation

Capital may shift toward jurisdictions with lower perceived sanctions exposure or more predictable compliance environments. Such reallocation can alter the regional structure of investment flows and reduce the competitiveness of affected financial centers.

Persistent asymmetry may contribute to structural capital divergence within the region.

6.2. Increased Transaction Costs

Enhanced screening procedures, additional compliance approvals, and extended transaction timelines increase the cost of cross-border operations. These frictions reduce transactional efficiency and may discourage complex or long-term investment projects.

Higher compliance costs can ultimately translate into reduced market attractiveness.

7. RISKS TO LISTINGS AND STRATEGIC INVESTMENTS

7.1. Listing Venues

Sanctions-related uncertainty may reduce the attractiveness of IPOs and secondary offerings. Issuers assess potential investor restrictions, liquidity limitations, and the risk of subsequent trading constraints.

Market perception of sanctions sensitivity may affect valuation and subscription dynamics.

7.2. Strategic Transactions

When structuring mergers, acquisitions, or long-term strategic investments, investors evaluate the risk of sudden regulatory restrictions, financing disruptions, or settlement constraints.

Sanctions asymmetry may therefore influence deal structuring, due diligence scope, and contractual safeguards.

8. INSTITUTIONAL BALANCING MECHANISMS

8.1. Principle of Proportionality

Sanctions risk assessment should reflect the actual legal status of the subject, the degree of involvement, and the existence of binding legal obligations, rather than relying solely on indirect or reputational signals.

Proportional application of controls supports both compliance integrity and investment neutrality.

8.2. Dialogue with International Partners

Regulators may maintain transparent communication channels with foreign supervisory authorities and financial institutions to reduce uncertainty and mitigate the risk of excessive market reactions.

Structured engagement contributes to greater predictability and coordinated risk management.

8.3. Explainable Compliance

Enhancing transparency in compliance decision-making, incorporating explainable AI tools, and maintaining documented risk assessment logic strengthen institutional credibility and reduce arbitrary outcomes.

Clear auditability supports confidence in regulatory and supervisory processes.

9. RECOMMENDATIONS

1. Develop supervisory guidance on managing sanctions asymmetry and its implications for financial stability.
2. Strengthen transparency of compliance decisions and sanctions risk assessment criteria.
3. Safeguard investment neutrality through consistent application of the proportionality principle.
4. Facilitate regional dialogue within APG and ASEAN on sanctions turbulence and cross-border risk coordination.
5. Integrate analysis of sanctions dynamics and compliance asymmetry into macroprudential resilience assessments.

10. CONCLUSION

Geopolitical turbulence presents new structural challenges for Asia's financial centers. Preserving investment neutrality under conditions of sanctions asymmetry requires institutional flexibility, transparency, and consistent regulatory communication.

Balancing adherence to international standards with the maintenance of competitiveness is a central determinant of long-term regional resilience.

The ARGA Observatory views this report as a contribution to the development of a sustainable model for managing sanctions asymmetry and preserving Asia's investment attractiveness.

APPENDIX A. TERMINOLOGY

Sanctions asymmetry — an imbalance between external sanctions regimes and domestic regulatory frameworks that creates indirect pressure on financial institutions.

Investment neutrality — a regulatory environment ensuring equal and predictable treatment for all investors.

Defensive compliance — excessively conservative compliance practices adopted in response to uncertainty and external risks.

APPENDIX B. INVESTMENT NEUTRALITY ASSESSMENT FRAMEWORK

1. Degree of financial system dependence on external sanctions regimes and global infrastructure.
2. Level of compliance burden associated with sanctions-related risks.
3. Impact of sanctions dynamics on investment flows and market liquidity.
4. Transparency and predictability of regulatory decisions.
5. Availability of review and appeal mechanisms in the application of restrictive measures.