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OP-ED CONTRIBUTORS | TRANSITIONS

Financial Time Bombs

By CHARLES DUELFER and JIM RICKARDS

THE economic crisis has made it painfully obvious that the United States economy has become very vulnerable to broken gears in the global financial system. But this is not simply a financial or economic problem — it is a grave national security risk, and our government must treat it as such.

Historically, Washington's national security and financial apparatuses have operated independently. Intelligence analysts have focused on explicit threats posed by weapons and conflicts. Those parts of the government charged with ensuring economic health have a different mind-set, monitoring capital markets where they assume threats are not malicious, but competitive in nature. This needs to change.

For a model, consider the evolution that took place in the 1990s with respect to cyber-threats. While this was initially the preserve of information technology experts and companies, government officials came to recognize the enormous potential threats to the power grid, the Internet and government computer systems.

In terms of economic security, however, a complicating factor is that financial experts and national security officials view risk in very different ways. The meltdown on Wall Street is largely a result of an overriding incentive to see risks as low. The group dynamic among financial houses was to lend more under more precarious conditions — if you didn't, a competitor would, and he would generate greater near-term returns, lure more investors and get a higher bonus.

Conversely, the national security community, tends to maximize risk assessments. Aerospace companies sell more weapons if the threat is judged to be increasing. National security analysts don't get jobs if they say there is no danger. It's all about playing up risk — sometimes too far, as the miscalculation over Iraqi weapons of mass destruction threat showed.

Despite these divergent views of risk, the talents of professionals in the capital markets and national security experts must be combined if America is to identify and respond to financial threats.

For example, while China has behaved appropriately during the global financial crisis, there is no doubt that its enormous reserves give it de facto veto power over some of Washington's interest

rate and exchange rate policies. What would we have done if Beijing had responded differently? And the desires of Russia (then fighting in Georgia) were a consideration during the Fannie Mae and Freddie Mac bailouts, because it is one of the largest holders of government agency debt.

Al Qaeda has declared that damage to the American economy is its second most important goal after mass casualties. Presently, who would warn the White House if foreign entities made a concerted attack on our financial system? Who is charged with detecting such activity?

The Obama administration needs to place a new priority on the national security implications of capital and commodities markets. The National Security Council needs to draw together the powerful talents and tools from segregated agencies to tackle the problem.

Our spy agencies alone lack the direction and specialized expertise to provide the real-time market analysis required. It calls for talent more likely found among hedge fund managers and open-market traders. After all, the data does not need to be captured clandestinely — much is readily available from exchanges, brokers and other open sources. Quick analysis — with the sorts of quantitative engines traders use, redesigned for national financial security objectives — may be the most critical aspect.

There is a tremendous range of global threat indicators that can be gleaned from careful scrutiny of trading activity. For example, in August 2006 an unexplained decline in certain airline stocks took place shortly before the arrests in Britain of terrorists plotting to blow up trans-Atlantic airliners.

The global financial meltdown is going to give our enemies new ideas to create economic havoc. We don't have much time to plan our response.

Charles Duelfer, the former director of the Iraq Survey Group, is the author of the forthcoming "Hide and Seek: The Search for Truth in Iraq." James Rickards was general counsel of the hedge fund Long-Term Capital Management and oversaw its rescue by the Federal Reserve.

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