Dollars *and* Diplomacy

When U.S. foreign policy bumps up against banking and finance.

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Beginning after the Second World War when the National Security Act was passed and the Bretton Woods institutions were launched, and increasingly in recent years, economic and particularly financial issues have routinely featured in defense and diplomatic planning. The U.S. dollar along with banking and securities industry positions have been key elements of soft power helping to drive foreign policy, and also acted as warning signals for potential threats and vulnerabilities at home and abroad to the national interest. Since the 1980s crises in developing countries, later termed "emerging markets," have been a preoccupation, with a shifting regional focus and emphasis on reconstruction and stabilization. Over the past decade front-line anti-terror states have drawn attention, and since September 11, 2001, the mission has been further adapted to concentrate on such areas as banking sanctions, cross-border payment tracking, infrastructure protection, and heightened screening of inward direct and portfolio investment.

Numerous agencies and departments are directly and indirectly involved in these questions in a supporting capacity for policy coordination and formulation. The list includes the U.S. Commerce, Defense and State Departments, and the Central Intelligence Agency, Federal Reserve, Office of the U.S. Trade Representative, Council

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of Economic Advisers, Agency for International Development, and Securities and Exchange Commission. However, the Treasury Department, through its international affairs function, and the White House's National Security and Economic Councils, with dedicated personnel working jointly and separately, are the primary responsible centers for articulation and debate.

The Treasury Secretary has long taken the lead in meshing and overseeing national and international economic policies. From the Nixon administration to that of George Bush senior, this dominance was formalized through Economic Policy Boards with the incumbent at the helm. In the early 1990s the model was superseded by President Clinton's creation of a stand-alone National Economic Council, with designated international deputies in charge, although resources from the outset have been devoted mainly to domestic fiscal and tax matters. Under this construct the Treasury Secretary remained top spokesperson, but the National Economic Council under Robert Rubin, its first director, conducted the daily outreach to multiple Council members in an effort to forge government-wide consensus. Early in this decade under President Bush, Treasury was also given a permanent seat on the National Security Council, alongside State and Defense, with his directive recognizing that "America's security depends on opportunity to prosper in the world economy."

Treasury's International Affairs department is the point unit assisting the Secretary and Deputy Secretary in managing a portfolio spanning debt, monetary, trade, and investment issues, and U.S. membership in development lending institutions such as the International Monetary Fund and the World Bank. It coordinates approaches with finance ministries worldwide, and prepares the annual G7 summit and related bilateral and multilateral meetings. It subdivides along geographic and functional lines overseen by deputies reporting to the Assistant Secretary and Undersecretary. Specific national security-related tasks are incorporated in its purview: an official chairs the Committee on Foreign Investment in the United States process for screening proposed acquisitions in strategic industries which was updated after the Dubai Ports controversy, and the Terrorism and Financial Intelligence staff joins with law enforcement and regulators to combat illicit money flows. It applies asset freezes and sanctions, and tracks targets including "rogue nations, weapons proliferators, cash launderers, and narcotics and terrorist facilitators."

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Emerging market currency crises have been a perennial battleground with the State Department, pitting pure foreign policy against technical financial sustainability objectives. Their spread from Mexico to Asia and Russia during the Clinton presidency triggered numerous accounts of bureaucratic and personal frictions. Interagency discussions pointed to Treasury's lack of geopolitical judgment, and to State's missing appreciation of capital and credit movements. Senior Treasury representatives, aided by Secretary Rubin's background and reputation, overwhelmingly guided the rescues. Although compromises were often struck, inherent conflict has lingered. In the present Bush administration, bilateral clashes and confusion have caused difficulties in planning and

Departmental Blinders

Former Treasury Secretary **Robert Rubin**

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executing reconstruction strategy in fragile states such as Afghanistan and Iraq. Congressional action through rival oversight committees has also fueled executive branch tension, especially in presumed specialist realms like "currency manipulation."

Throughout its history, the NSC has called on both outside and in-house international economic expertise, but it was relegated to secondary status until the end of the Cold War, when the substantive component was routinely woven into the traditional regional assignments of staff directors. With promotion to full member of the body, Treasury's profile has been raised, with major engagement in Iraq on currency conversion, debt reduction, and aid, and on Iran with business and banking boycotts. The dedicated personnel complement has expanded under the Bush Administration, and the national security adviser has an international economics aide with the title of Deputy Assistant to the President. Responsibility is shared with a counterpart at the NEC, continuing the joint chair practice begun on the latter's launch.

The NEC originally organized its own agency and cabinet working groups on transnational issues, trade, and finance, the last with Treasury in the lead. The liaison with NSC was often more personalized than institutionalized, with differences in the formality of processes that could be circumvented altogether on subjects like Russia, where top authorities elsewhere in government were close to the President. NAFTA passage was an early NEC-facilitated success, and soon after formation it also convened officials from NSC, State, Treasury, and CEA to set options with environmental experts for the Kyoto Treaty climate negotiations. Free trade agreement preparation and promotion for national security goals has subsequently been a steady dual Council theme, from China's WTO entry to recent attempts to complete pacts in Colombia, Korea and the Middle East. The two have selectively weighed in on financial rescues, most recently for Latin American countries, where they tend to defer to Treasury.

In reviewing the past fifteen years' experience, many observers argue that the Clinton more than the Bush Councils tackled international economic and financial questions. However, now dealing with the spread of the global credit crunch and recession, rising energy and food prices, and the new power of sovereign wealth funds, the outgoing Administration may have shifted the balance. Nonetheless, their respective emphasis has remained on the conventional and then wartime international affairs agenda, and domestic program reform such as in health care and social security.

A 2005 report by a Princeton University Working Group on Economics and National Security, comprised of many former officials, concluded that the formal interagency framework may have done "a reasonably good job" of ensuring "seats at the table," but that *ad hoc* policy meetings within a limited circle could exclude needed input by circumstance or design. It called for greater integration and cited existing gaps in understanding and addressing the evolution of China and Asian competition.

Unquestioned U.S. economic and financial dominance which prevailed for decades has yielded to today's more complex challenges involving multiple public and private sector actors and capital and commercial channels. National Security Strategy documents stress worldwide growth and poverty reduction as core pillars which should catalyze Treasury, NSC, and NEC commitment. Treasury's scope and status have been enhanced, but lines blur with State even on technical topics like debt restructuring. Collaboration and synergy could benefit from written mission agreements that clarify exclusive and lead roles. Simultaneous international economics coverage by the Councils may be redundant and invite fragmentation rather than alignment, with the NEC's comparative youth an institutional disadvantage. Issue priority may be obstructed by the dedicated deputy's subordination to the NSC adviser.

A procedural and substantive fix would be creation of a separate global economic adviser to the President, consolidating the relevant staffs at the highest White House echelon. At the same rank, a specialist finance aide should be named by presidential decree, reflecting the distinct nature and headline importance of these issues. This office would supplement Treasury views, and enshrine a broad overdue banking and securities market capacity in the national security apparatus. ◆