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# Money and Terrorism; Strategic Insights, v. 3, issue 4 (April 2004)

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# Money and Terrorism

## *Strategic Insights*, Volume III, Issue 4 (April 2004)

by [Loretta Napoleoni](#)

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U.S. Secretary of State Colin Powell recently acknowledged that the life-line of terrorists is money. Two and a half years since 9/11 it has become apparent that economics, not politics or ideology, is the engine of the armed struggle. This is the unexpected and disconcerting truth unveiled by an economic analysis of five decades of modern terrorism.

During the period of decolonization after WWII, armed organizations were economically dependent from rich sponsors, i.e. former colonial powers. In 1949 in Indochina, France trained and bankrolled the *Maquis*, a guerrilla army whose aim was to contain Soviet expansion in the French colonies.<sup>[1]</sup> State sponsored terrorism became a familiar feature of the Cold War. The United States and the Soviet Union funded terror groups to fight wars by proxy on the periphery of their own spheres of influence. The high cost of this type of war, coupled with its unpopularity at home, forced Western powers to resort to a mixture of legal and illegal revenues to channel money overseas. In 1984, amid widespread opposition to America's involvement in Nicaragua, the Reagan administration managed to get Congressional approval for a financial aid package of \$24 million, which was used to arm 2,000 Contras. Although this figure was increased every year thereafter until the Iran-Contra scandal erupted, it was insufficient to meet the high costs of bankrolling the Contras. To bridge the gap, several covert operations were put in place. Oliver North set up a scheme to defraud U.S. insurance firms and banks, generating close to \$1 billion per year for the Contras. In another illegal project, U.S. weapons acquired by the CIA were sold to Iran, using Israeli and Saudis businessmen, who charged handsome fees, as brokers. Iranian payments were then channeled through numbered Swiss accounts controlled by the Contra leadership.<sup>[2]</sup> Unsurprisingly, American taxpayers ended up paying for the cost of both legal and illegal funding; the full economic burden of state sponsored terrorism always falls on the domestic economy of the sponsor.

Terrorism has always been an expensive business to run. In the mid 1970s, the Red Brigades, the Italian Marxist terror group, had a yearly turnover of \$8 to \$10 million,<sup>[3]</sup> equivalent to that of a medium to large size commercial enterprise operating in the industrialized regions of the north of Italy. Unlike the U.S., which was cash generous, the Soviet Union never funded Marxist groups directly, supplying them instead with free training, arms and ammunition. Groups like the Red Brigades and the Baader Meinhof Gang had to raise their own cash. This required managerial finesse more than military expertise.

### **The Shell-State Game**

The willingness to gain financial independence from their sponsors, coupled with the rising cost of terrorist activity, motivated armed organizations to find ways of becoming self-sufficient. In the 1970s, Yasser Arafat masterminded the transition of the PLO from a state-sponsored to an economically independent armed group by developing the first model of what has become known as the privatization of terrorism. During the civil war in Lebanon, Arafat assembled the Palestinian

state-shell, a de facto state held together by a well developed socio-economic. Over the last 30 years, similar shell-states have blossomed in war zones and in places where there is a high degree of political instability. Colombia, Peru, Chechnya, Afghanistan, and today Iraq have become ideal breeding grounds for these entities. Terror groups gain military control of the territory and proceed to destroy the existing socio-economic infrastructure, or what is left of it. Their final aim is to replace it with the armed groups' own socio-economic infrastructure, an economic system created exclusively to feed the armed struggle. The 2003 attacks against the UN and the Red Cross in Iraq are part of this strategy.

The key to the survival of the shell-state rests upon the management of its finances, and on its interdependency with traditional economies. The Palestinian shell-state was run as a de facto legitimate state; for example, a five-percent income tax was levied on Palestinians working abroad. The Arab states where Palestinian workers resided were held responsible for collecting the tax. Legally and illegally generated money was then invested in legitimate activities through the international financial markets. In 1976, following the legendary bank robbery of the British Bank of the Middle East, Arafat chartered a flight and took the PLO's share of the loot to Switzerland, to invest it; the Christian Phalange and the Corsican mafia, the other partners in the robbery, used their shares to buy arms.

CIA estimates show that in the 1990s the PLO's total wealth ranged from \$8 to \$14 billion. If we take this figure as a rough estimate of the GDP of the PLO, then at the time it was higher than the yearly GDP of several Arab countries, including Yemen (\$6.5 billion), Bahrain (\$6 billion) and Jordan (\$10.6 billion).<sup>[4]</sup> As Palestinian wealth grew, so did its interdependency with the economy of its neighbor and enemy, Israel. In 1987, the Israeli finance minister Adi Amorai released a PLO courier who had been stopped at the Allenby Bridge, the transit point between Jordan and Israel. The man was carrying a suitcase with \$1 million in cash. Amorai knew that the money would be exchanged for shekels and spent inside Israel, an injection of cash that the inflation-ridden Israeli economy badly needed.<sup>[5]</sup>

### **Terror Money Goes Global**

In the 1990s, the further deregulation of international economic and financial markets made possible the globalization of terrorism. As economic and financial barriers came down, armed groups linked up economically and become transnational, that is, they were able to raise money across borders and to operate in more than one country. The business empire of Osama bin Laden, whose profits bankrolled terror attacks against Western interest across the Muslim world, is a striking example of this phenomenon. His portfolio is truly transnational and highly diversified.

The globalization of terrorism greatly increased the interdependency between terror money and traditional economies. While residing in Sudan, bin Laden acquired seventy percent of Gum Arabic Ltd., a company which held eighty percent of world supply of this product<sup>[6]</sup>, a virtual monopoly. By far the largest importer of gum arabic is the U.S., which enjoys a special price agreement with the supplier. In 1998, the Clinton administration's decision to impose economic sanctions on Sudan met with opposition from lobbies representing U.S. importers of gum arabic. Eventually they convinced the administration to exclude it from the list of sanctioned products. Their argument was very simple: the sanctions would hurt American importers. Why? Because the Sudanese would simply sell the product to the French, the second largest importer, who in turn would offer it to the Americans at a premium.<sup>[7]</sup>

Terror leaders are well aware of the degree of dependency between traditional economies and the New Economy of Terror, the international economic system run primarily by armed organizations to self finance the armed struggle. In 1990 bin Laden issued a *fatwa* urging his followers to refrain from attacking Saudi Arabia because the revenues from the oil industry were needed to consolidate the Islamist revolution. These revenues came from legal businesses, run

by Saudis who backed al Qaeda. They found their way into the New Economy of Terror via donations or share of profits, which are not illegal activities.

Western corporations are also often aware that they are doing business with groups closely linked with the illegal and terror economy. One way Islamist armed groups fund themselves is by smuggling of electronic products in Asia. According to Daniel Pearl, the *Wall Street Journal* reporter kidnapped and killed by *Jaish-I-Mohammed* (Army of Mohammed) in Pakistan, Sony Corporation used a contraband network in Asia as a part of its overall strategy in the region.<sup>[8]</sup> Consumers are also dependent on terror money. In the Tri-Border region of Latin America, Arabs linked to Hamas and the Hezbollah run a buoyant money-laundering business of drug funds through smuggling of duty free products from Central America. This activity supplies the Colombian population with foreign goods that they otherwise could not afford.

## Impact and Conclusions

By far the most damaging effect of the deregulation of markets has been the merging of the New Economy of Terror with the international illegal and criminal economy. Today they amount to about \$1.5 trillion, higher than the GDP of the United Kingdom. This money is evenly divided into three sectors:

- \$500 billion in capital flights, money which moves illegally from country to country, undetected and unreported <sup>[9]</sup>
- \$500 billion in what is commonly known as the Gross Criminal Product, money generated primarily by criminal organizations <sup>[10]</sup>
- \$500 billion in the New Economy of Terror—money produced by terror organizations—of which as much as one third is represented by legal businesses and the rest comes from criminal activities, primarily the drug trade and smuggling <sup>[11]</sup>

The bulk of this \$1.5 trillion flows into Western economies, where it gets recycled in the U.S. and in Europe. It is a vital element of the cash flow of these economies.

Even more shocking is the discovery of the interdependency between the terror/illegal economy and the U.S. money supply. The means of exchange of this economy is the U.S. dollar, in particular \$100 bills. Arms, drugs, smuggling of people, and other illegal activities are cleared in U.S. currency. Therefore the rate of growth of this economy is roughly indicated by the yearly infusion of new U.S. dollars. Recent studies from the Federal Reserve in St. Louis show that since the 1960s the stock of new dollars issued in the U.S. and taken abroad for good has been steadily rising.<sup>[12]</sup> In 2000 as much as two thirds of the U.S. M1, equivalent to \$500 billion, has been taken out of the U.S. monetary system and is held abroad.<sup>[13]</sup> This figure does not include stocks of dollars held by central banks in the form of reserve currency. If these statistics are correct, then the rate of monetary growth of the terror/illegal economy is higher than that of the U.S. economy.

Because the U.S. dollar is considered the reserve currency, the stock of dollars held abroad is a considerable source of revenue for the U.S. Treasury through seignorage. In other words, the U.S. Treasury can issue T-bills and borrow against the total stock of dollars held in the world, not just on the stock held inside the U.S.. This amounts to a considerable tax write-off.

To conclude, the interdependencies between Western economies and the illegal/terror economies are so deeply rooted that unilateral measures to sever them may actually backfire. The Patriot Act, for example, has had an impact upon the dollar. The recent fall in the value of the dollar seem to be related to a new tendency of both legal and illegal businesses in Asia and Africa to denominate their transactions in dollars. Switching to the euros avoid the restrictions imposed by the Patriot Act and allows the illegal/terror economy to continue growing. Any attempt

to curb the international illegal/terror economy will have to take into consideration these interdependencies and be the result of a concerted multilateral strategy.

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## About the Author

Loretta Napoleoni is the author of *Modern Jihad: Tracing the Dollars Behind the Terror Networks*, a book on the economics of terrorism. She is an economist who has worked for banks and international organizations in Europe and the U.S.. In the 1980s, she worked at the National Bank of Hungary on a project on the convertibility of the forint, which later on became the blue print for the convertibility of the ruble. She has written novels and guide books and translated and edited books on terrorism. In the 1990s she was one of the few people to interview the Red Brigades after three decades of silence.

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