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From: Lloyd Etheredge <lloyd.etheredge@policyscience.net>

Subject: 249. Red Team: An urgent economics question that only the DNI's system can answer: "One Billion Threatened by Hunger." Recommending an All-Competing-Theories, Multi-Method, Rapid Learning Project

Dear Dr. Fischhoff, Dr. Hauser, Dr. Atkinson, Dr. Nordhaus and Colleagues:

I write to express concern that there should be a Red Team/National Academy project already underway to upgrade models and policy options concerning global commodity prices. Something serious and unexpected is happening.

There are urgent questions that only America's DNI system [including its databases, the ability to access internal information that institutions want to keep secret, and - perhaps - the new analysis methods for financial markets that the CIA was tasked to develop quickly] can answer. [As background I enclose the recent article, "Chronic Hunger to Affect 1bn People," by the Financial Times commodities correspondent Javier Blas. This may soon count as a global economic catastrophe, too - and nobody seems to have predicted this one, either.] The National Academy of Sciences should push the red "Alarm" button and recommend an urgent Red Team reconsideration of conventional ideas.

Conjectures without Proof

Also: for non-economists it is important to under-score that prices are both high and very volatile. “Highly volatile” means that none of the standard fixed-coefficient regression models works reliably - i.e., in a sense, the causes could be anything. A corollary is that while unnamed “experts,” journalists, and columnists conjure with different explanations, few people cite numbers or coefficients or trace the processes of cause and effect with convergent evidence. Nobody - yet - has proof.

General Clapper’s senior staff will recognize, in many explanations, the possibility of the same disinformation that sophisticated publicists gave to Congress and the media in the run-up to the last global economic catastrophe, to the still-mysterious \$4/gallon gasoline bubble, etc. The dust cloud of proffered explanations must have a shred of plausible truth, but the explanations are chosen so that nobody has the capacity [i.e., the capacity that the DNI’s yottabyte, 10 to the 24th system, and spycraft possess] to check reality themselves, the actual strength of the effects, and the processes by which future commodity prices are thereby changed via specific actors. “Supply and demand” is a phrase that can be used, with a hand-wave, to explain anything. When Krugman conjectures about the unexpected hoarding behavior of individual Chinese peasants, or somebody waves their hands and blames “bio-fuel” or “rising demand by x,” or “global warming” or “the unusual weather in. . . .” a Red Team/National Academy project might be shocked by the lack of proof for these public, conventional explanations of food prices, etc. Even Krugman admits that he receives more vigorous, skeptical challenges from his readers about today’s news media explanations than almost any other topic.

A Warning: Hedge Funds are Back. Does Director Panetta Really Know What They are Doing?

An additional reason to be skeptical of conventional wisdom - and why pressing the international public sector to pay very large sums in sudden, humanitarian appropriations may be unnecessary (if the true causes are known and addressed quickly) - is that hedge funds are back! Their net worth has returned, and also their fabulous profitabilities. [In just the second half of last year, the top 100 hedge funds made \$70 billion in profits for investors; the top 10 made \$28 billion - in both cases, after paying an average of 20% of profits to the management team - see

James Mackintosh, “Investing Stars Lead Bumper Year for Hedge Funds” Financial Times, 3/1/2011.] But - if it is not producing real estate bubbles in the US and several other countries - where is this money going? What are they up to? And are selected commodities - like food, that will raise the threat of malnutrition to 1 bn people and cause deaths (according to the World Bank) of tens of millions of vulnerable infants and children in the poorest UDCs - being manipulated so unethically for large profits? Are the global financial Titans chagrined and chastened by what happened last time? Or are they starting the next cycle, and doing it again? Only the DNI can tell us - and President Obama.

- Volatile markets (like commodity markets) are highly attractive to hedge funds because hedge funds can become fabulously wealthy if, statistically, they invent any methods that allow them to forecast the volatility even slightly better than chance. Hundreds of millions of dollars can move in fractions of a second, and one strategy of hedge funds is to bet huge sums that net pennies, or fractions of pennies, per share. Also: Forecasting trends does not necessarily mean guessing prices days or months in advance. The systems are automated and driven by super-computers that can continually test market trends by dozens of experiments/second and profit from trends in micro-fluctuations.<1> The actual causes of rising prices may include causes that are artifacts of many highly sophisticated computerized algorithms around the world and - until the DNI discovers what algorithms are being used and runs its own scientific simulations - even the members of the National Academy of Sciences cannot predict what will happen. A new meta-system may be mutating with logics and collective impacts on the world that the software designers did not anticipate would shift 1bn people into hunger.

Global political Instability and American lags

By now, I would have hoped that a solid, multi-method, DNI/CIA research project, testing all major competing ideas, had been completed and that off-the-record briefings were allowing the American public, and a wider network of the World Bank, other IGOs and other governments, to understand the proven causes. [The French government probably does not have the data and intelligence resources to nail this problem by itself.] The DNI system is supposed to connect the dots. But, instead, is this new global challenge, that requires an unusual range of scientific and real-world expertise, falling between the cracks?

The Islamic Connection

- The Islamic connection adds urgency for the Red Team/National Academy of Sciences all-competing-theories, multi-method, rapid learning project. As Friedman has noted (my submission # 222 archived at www.policyscience.net at II. D), high food prices are contributing to political instability and violence across the Islamic world. And there is nothing that overthrowing autocrats and shifting to democracy can do to change this new source of fear and anger in UDCs.

Unfortunately, the American news media are not giving prominent coverage to rising and volatile food and other commodity prices on global markets (except for gasoline in the US.) Consumers in wealthy countries like the US spend a much smaller fraction of personal income on food and, because so much of the food is processed, the basic commodity price typically is 25%, or much less, of the retail cost.

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<1> In the 1980s, when I was Director of Graduate Studies for International Relations at Yale, I often recommended that my MA students with math aptitude take a graduate course in International Finance. One of my students returned in the fall - thrilled! - because his graduate course had landed him a Wall Street summer job. He had helped to figure-out the behavior of the Russian government and its central bank. As bureaucracies, they were regular and predictable about certain major market transactions - days of the months, even times of the day in Moscow. He developed a system to bet large sums on the micro-effects and he made enough money for his company that he paid for his two years of graduate education and built a future career plan in two months of work.

Chronic hunger to affect 1bn people

By Javier Blas, Commodities Editor

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The number of chronically hungry people is approaching 1bn, the level last seen during the 2007-08 food crisis, in the clearest sign yet of the humanitarian impact of rising agricultural commodities prices in poor countries.

Robert Zoellick, World Bank president, said on Tuesday that the rise in food prices had already pushed an additional 44m people into extreme poverty, which is closely associated with hunger.

The rate of the increase suggests the number of undernourished people, which the UN said last year was 925m, will now hit 1bn by the end of this year as the effect of spiralling prices filters through.

“The trends towards the 1bn are worrisome,” said Mr Zoellick. “Global food prices are rising to dangerous levels. The price hike is already pushing millions of people into poverty and putting stress on the most vulnerable, who spend more than half of their income on food.”

The rise comes as G20 finance ministers are due to meet in Paris on Friday to discuss ways to tackle soaring prices, which are driving inflationary pressures. France has put global food security at the centre of its G20 presidency.

Brazil adopted a tough stance on the issue on Tuesday.

“Brazil totally opposes the use of mechanisms to control or to regulate the price of commodities,” said Guido Mantega, the country’s finance minister. “Most of the prices of these commodities will fall naturally as the market re-establishes itself.”

However, France is stopping short of proposals to regulate prices directly, and is instead pushing for tighter controls on speculators, restrictions on the use of export bans and better information on grain stocks held by important exporting and importing countries.

The World Bank and the UN use different methodologies to estimate extreme poverty and chronic hunger, but analysts say they usually go hand in hand.

The number of chronically hungry people surpassed 1bn – about one in six people on the planet – for the first time two years ago. Before that crisis, there were some 850m chronically hungry people in the world, a level that has been about constant since the early 1980s.

Mr Zoellick said the rise in food prices, coming so soon after the 2007-08 crisis, suggested the world was not dealing with a “one-time event”. Rather, long-term demand was likely to keep upward pressures on prices for “years to come”.

The prices of wheat, corn and soyabeans have hit 30-month highs over the past few days after bad harvests, export restrictions, extremely low inventories and soaring demand in emerging countries and for bio-energy in the US and Europe. But officials are drawing comfort from relatively stable prices for rice, one of the two most important farm commodities for global food security and the staple for 3bn Asians.

In addition, good harvests in many African countries are keeping local prices stable, even as international wholesale prices skyrocket. Experts say both factors have mitigated the social effect of rising prices.

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