

Market Update Call – Audio Transcript February 23, 2016

Speakers:



John M. De Clue, CFA
Chief Investment Officer
The Private Client Reserve



Harleen Gambhir
Counterterrorism Analyst
Institute for the Study of War

Opening: This is a recording of the U.S. Bank Wealth Management Market Update Call held on February 23, 2016. The discussion featured insights on one of the most complex and dangerous regions in the world: the Middle East.

John DeClue: Hello and welcome to our Market Update Discussion, which is hosted by U.S. Bank Wealth Management. I'm John De Clue, Chief Investment Officer for The Private Client Reserve of U.S. Bank.

As we all unfortunately know, turmoil in the Middle East continues to weigh on geopolitical security, and frankly is undoubtedly having an impact on the investment markets worldwide.

With this in mind, we're delighted to once again have an expert on the region to discuss with us recent events and what we might expect going forward. Please join me in welcoming our special guest Harleen Gambhir from the Institute for the Study of War, or ISW as I'll call it going forward. Thanks for joining us, Harleen.

Harleen Gambhir: Thank you so much for having me.

Investment products and services are:

NOT A DEPOSIT	NOT FDIC INSURED	MAY LOSE VALUE	NOT BANK GUARANTEED
NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY			

John DeClue: Harleen is a graduate of Harvard University and she serves as a counterterrorism analyst at ISW. For those of you that might not be familiar with ISW, it's a nonpartisan, nonprofit public policy research organization based in Washington D.C., with a mission of promoting an informed understanding of war and military affairs through comprehensive independent and accessible open source research and analysis. Since we're in an election year, I should also stress, and ISW has asked me to stress, that they are strictly nonpartisan and actively brief Republicans and Democrats, including both those in office and those running for state and national office.

At ISW, Harleen focuses on the Islamic State of Iraq and al-Sham in terms of their global strategy, better known as ISIS or ISIL, and its operations, as well as U.S. national security interests encountering ISIS's caliphate. She is frequently featured in the media, including appearances on CNN, MSNBC, and Al Jazeera America and has been published in *The Wall Street Journal*, *The Washington Post* and other leading publications.

Before I turn to Harleen with my first question, please keep in mind that the views she may express are, of course, those of ISW and do not necessarily reflect the opinions or positions of U.S. Bank.

We were very happy to have your colleague, Jessica McFate on the line just about a year ago from ISW. So thank you for coming in and talking to us about a year after our call with Jessica.

A lot seems to have happened in the past year. Maybe the best way to start is to ask you to do a quick compare and contrast about where the ISIS threat stands today as opposed to last year at around this time?

Harleen Gambhir: I think the past year, and all the turmoil therein, has really shown us that the ISIS threat is intertwined with a whole host of different conflicts that we've seen unfolding across the Middle East. And as those conflicts have intensified, the subject of how to address ISIS, how to defeat ISIS, will become more and more complex.

What I'll do is just go over a few of the major time ticks, the major markers of really significant changes that we've seen over the past year.

The first is March 2015, when we saw ISIS launch its first major attacks in Yemen and, more importantly, Saudi Arabia, with the help of an Arab coalition that actually invaded Yemen, heightening a regional sectarian conflict that was already being fought in Syria. That really helped to intensify this overall sectarian warfare that has been creating an environment in which ISIS and Al-Qaeda have both been thriving. That proxy war obviously received another boost in July 2015, when we saw the passage of the Iranian nuclear deal.

From there the possibility of lifting sanctions, I think, really has allowed Iran to approach its military engagements outside of its own lands more

enthusiastically and has, furthermore, sort of heightened Iran's involvement both in the Syrian conflict and in terms of support to fighters in Yemen.

And then finally, of course, we had Russia enter the Syrian conflict in September 2015, which really was a fundamental shift, and I think has incredible implications for both the trajectory of the Syrian Civil War and also for ISIS's chances of survival both in Iraq and Syria and more broadly in the region.

We saw, with Russia's entry, that Russia achieved its goal of establishing an air and naval base on the Mediterranean, which gives it a way to threaten Eastern Europe and really pressure NATO (North Atlantic Treaty Organization) more broadly, particularly through attacks and rhetorical positioning against Turkey. And then we also saw that Russia's entry into the conflict has really bolstered Syrian President Bashar al-Assad, who is fighting against a widespread opposition.

That shift, Russia's entry into that conflict, has really ensured that that conflict is going to continue on for quite some time, thereby creating an environment that makes ISIS's prospects for staying in the region quite good because it will have that continued area of conflict in which to keep its safe haven and continue its efforts to expand regionally.

In summary, looking back over this past year, I think we've seen: one, the heightening of that regional sectarian conflict; and two, the introduction of new actors that will ensure that those conflicts continue, thereby creating a condition in which ISIS is likely to thrive.

John DeClue: You follow ISIS globally, of course, which basically means outside the areas of Iraq and Syria. I think most people might be under the impression that ISIS has been pretty quiet outside of Iraq and Syria until, perhaps, the Paris attacks. Is that true or have they been more active than we might think?

Harleen Gambhir: They have. ISIS has actually been pursuing a global strategy, at the very least, since the establishment of its caliphate in Iraq and Syria in June 2014, if not before then.

ISIS is very clear about its grand strategic objectives, which are to expand the caliphate that it believes it has already declared, to encompass all Muslim lands, and then to provoke and win an apocalyptic war with the West.

So in pursuit of those objectives, ISIS is pursuing a global strategy consisting of three parallel campaigns. The first is its campaign within Iraq and Syria to defend the caliphate and ISIS has actually been doing quite well with that. It's essentially unchallenged in its core terrain in Eastern Syria and Western Iraq, though it obviously is facing opposition around all the corners from Kurdish forces, the Iraqi security forces and some U.S.-backed Syrian rebels. But we've seen that it's been able to hold on to its caliphate terrain, which is incredibly important to its own claim of legitimacy. And it's also been able to launch, as we've seen in the past few days, very significant asymmetric

attacks in Western Syria, weakening the Syrian regime in hopes of further expanding westward.

At the same time, ISIS is executing a campaign in the broader Middle East, North Africa and Central Asia regions, working to establish affiliations with jihadist groups helping to develop both their military capability and also their capacity for brutal social governance and control, and helping them really expand ISIS's caliphate by acting in ISIS's own image.

Those groups are also working to exasperate disorder regionally; working to undermine existing stable states and also exacerbate ongoing conflicts in preparation for ISIS's desired expansion outside of Iraq and Syria. So, we've seen since November of 2014, ISIS has declared official affiliates in Algeria, Libya, Egypt, Sinai Peninsula, Saudi Arabia, Yemen, Nigeria, Russia, Afghanistan and Pakistan.

Those affiliates vary in strength. The most threatening ones are in Libya, Afghanistan and Egypt. But each of those actors have been making efforts to, in some way, really heighten the overall level of global disorder and promote ISIS's resiliency outside of Iraq and Syria. And in particular, we've seen that ISIS's affiliate in Libya has had significant success in this regard. Not only taking control of terrain and governing a city, but also launching attacks against oil infrastructure and receiving reinforcements of ISIS's leadership from within Iraq and Syria. All told, creating something of a second safe haven for ISIS outside of Iraq and Syria that will ensure that defeat in Iraq and Syria, alone, will not directly translate into ISIS's overall defeat, which is definitely an important consideration for the United States, that's reassessing and assessing its strategy against ISIS.

The final campaign that ISIS is executing is a campaign against the West, against the broader world. That's the campaign of both encouraging lone-wolf attacks and also of directing and resourcing more sophisticated attacks as we saw, obviously, in November of last year in Paris. And ISIS actually has a fairly nuanced objective that it's pursuing with that campaign. It's not only to punish the actors that are working against it in Iraq and Syria, it's actually trying to polarize and destabilize the West, and in particular Europe. ISIS hopes that its campaign of attacks will incite state and social responses that will alienate Europe's Muslim population, increase recruitment to ISIS and, overall, create cultural divides that will sort of prepare that battlefield for ISIS's desired apocalyptic war.

John DeClue: How would you handicap their success? And then secondly, what do they really want and are they achieving their goals, in your opinion?

Harleen Gambhir: ISIS is achieving its fundamental goal. It's been able to hold on to its terrain within Iraq and Syria, even though, as I mentioned, it has these multitudes of enemies that are working against it. And, I think, that's in part because ISIS really isn't at the top of anyone's priority list within this grand anti-ISIS coalition that the United States has assembled.

Because of the sectarian proxy war, Iran, as well as Saudi Arabia and other regional actors, are more focused on positioning themselves against each other. And that's created an environment in which ISIS has been able to endure and has been able to continue its claims that it has the caliphate. And it's also achieved fairly significant success in setting up precedents for other jihadist groups, which is very significant. Its own sort of style of very brutal governance and top-down military control has really changed the way that certain jihadist groups are acting, and I think it doesn't bode quite well for what we would expect in the future.

John DeClue: We've seen isolated incidents of ISIS attacks in the United States, San Bernardino being the most tragic, I guess, and significant. What threat does ISIS pose in the United States? And then continue on in terms of threats to our allies, Europe for example?

Harleen Gambhir: ISIS primarily threatens the West through lone-wolf attacks. As I mentioned, in its sort of campaign at the West, there's both encouraging, inspired attacks and then also directing attacks. And we've seen, obviously, not only with the San Bernardino attackers, which was an example of a successful attack, but in the multitudes of pro-ISIS arrests and investigations, which are ongoing, as the FBI director has said, in 50 states, that ISIS actually is gaining resonance among certain fringes of our society, and are able to radicalize individuals and convince them that in order to defend the caliphate they need to act. That's an ongoing threat that really is heightened by the fact that ISIS continues to have this terrain within Iraq in Syria that it can claim as actually symbolic of a new area of Islamic governance.

The threat to Europe is actually much greater and much more immediate. Obviously that is made very clear by the November Paris attacks, but remains a continuing threat stream that we've seen; that ISIS has been attempting to send attackers in through the refugee flows in Europe, but also enjoys fairly widespread existing networks across multiple European countries that it has been working with to try to resource and facilitate explosive and spectacular attacks in Europe.

On one hand, it has those capabilities and on the other hand, ISIS is particularly poised to asymmetrically harm Europe because of the multitude of pressures that Europe is under right now. It's obviously facing financial difficulties. We're seeing the pressures that the refugee flows are placing on Europe. And then at the same time, we're having this ongoing discussion about the future of the Schengen zone and the future of the EU (European Union) while Russia is also trying to push against the idea of the EU and weaken that alliance. And so, ISIS's efforts to destabilize and polarize, as I mentioned, to really push, to exacerbate the cracks in European society, could have more resonance than usual. And I think that really should cause concern.

John DeClue: Looking forward, in terms of what we might expect to see from ISIS, particularly outside of Iraq and Syria, where are they already active and we're not paying enough attention?

Harleen Gambhir: That's a good question. ISIS has been hinting and actually is a very useful actor to study because it often will telegraph where it intends to go and then will actually go there. It actually makes it possible, from the open source, to analyze its intent and capability in a certain area. We've seen that ISIS really does intend to expand its regional affiliate campaign further, beyond where it's been operating thus far in three specific areas.

The first is Tunisia, where ISIS has launched two terrorist attacks in 2015; the first at the Bardo Museum and the second at a resort in Sousse, Tunisia, using the base that it's established within Libya; ISIS very likely intends to continue launching those destabilizing attacks, with the intent of actually using its fairly significant Tunisian fighter bases, which are currently based in Iraq and Syria or Libya to actually establish an affiliate in that country once the conditions are ripe.

The second location is Bangladesh, where there's a fairly active attack cell that has been launching ISIS claimed attacks about once a month against non-Muslim targets. A Christian priest, in the past two days. A Hindu priest, and a Italian missionary. Essentially both proving its existence and location and also, we think, intending to sort of show up Al-Qaeda in the Indian subcontinent, which is Al-Qaeda's affiliate in Bangladesh.

And then the third location is Southeast Asia more broadly. And particularly we're looking at Indonesia, Malaysia and the Philippines as areas where we've seen militant groups pledge their allegiance to ISIS and really jockey amongst each other for ISIS's blessing or attention in order to push for a formal affiliation. We saw, obviously, on January 14 an ISIS-claimed attack in Jakarta. But even prior to that, we've seen that Indonesian militants who are with ISIS in Syria have actually been sending resources back home, trying to develop those militant networks further and push towards greater cohesion so ISIS can formally expand.

John DeClue: Let's talk about Syria for a minute because it's been very recently in the news, and everyone is looking at it now. We have attempts at peace talks, cease fires, semi-cessations of hostilities, a lot of diplomatic movement positioning in that regard, but a lot of military activity as well by the Syrian regime and Russia.

I note that ISW, your firm, has a new series of reports that says ISIS isn't the most dangerous group in Syria. So you're going to have to explain that.

Harleen Gambhir: A take away that we've observed at ISW and also with our partner organization, the Critical Threats Project at the American Enterprise Institute, is that ISIS's activities, its actions, which are gaining so much media attention and so much government attention are actually providing cover for Al-Qaeda – both regionally overall through these affiliates and especially in Syria where ISIS is operating in addition to Al-Qaeda Syrian affiliate Jabhat al-Nusra.

What we've seen is, as the United States-led anti-ISIS coalition is framing its strategy as solely an anti-ISIS strategy, Jabhat al-Nusra has been taking

advantage of that situation and in particular, working to buffer itself against the weaknesses that ISIS has against the idea of a Sunni awakening, as we saw in the fight against ISIS in Iraq. So, Jabhat al-Nusra is building its relationship amongst the Syrian opposition, making sure that it is able to gain popular support while pursuing Al-Qaeda's objective, which is very similar to ISIS's objective, of establishing an Islamic caliphate and defeating the West. The two share the same end goal, though obviously different methodology.

Jabhat al-Nusra is sort of working under the radar to make itself invaluable to the Syrian opposition, including to elements of the Syrian opposition that the United States would likely want to work with in a fight against ISIS. And as it's working to intertwine itself, we're seeing that Jabhat al-Nusra is really positioning itself to be able to expand in a very frightening way if and when ISIS is defeated in Iraq and Syria.

And so the danger that we're facing now, as the United States is formulating its strategy and is working towards ISIS's defeat, is that we could very well likely get a situation in which ISIS is actually deprived of this area of control and where it's pushed on the map to be defeated, but then Jabhat al-Nusra, the Al-Qaeda affiliate, is standing in the wings ready to take advantage of that and ready to declare an Islamic emirate for Al-Qaeda in Syria.

John DeClue: Interesting. One final question, Harleen, how should we, in the United States and our allies, change our approach, if at all, to countering ISIS?

Harleen Gambhir: We absolutely need to be formulating a strategy that is not just an anti-ISIS strategy because there is such a danger of inadvertently empowering Al-Qaeda. The United States needs to be making sure that whatever it does against ISIS actually doesn't empower Al-Qaeda and then, even further than that, actually fights against Al-Qaeda in Syria.

The other takeaway I think, is that currently U.S. strategy is very focused on specifically targeting attack nodes. I think we've seen that over the past week as we've had these strikes in Libya, that the administration is working primarily to fight against and to target Al-Qaeda and ISIS elements that are actively plotting attacks against the West. But really, it is the safe haven within Iraq and Syria, both for ISIS and Al-Qaeda, that is empowering these groups. So, retaining that focus on working against those groups, organizations' sources of strength is really critical.

I think the most important thing, as we've seen in recent days, is the Sunni regime and Russia have been working to encircle and besiege Aleppo, one of the last bastions of the Syrian opposition. And the moderate Syrian opposition is that we need to make sure that there actually is a non-Salafi Sunni element of Syria that we can actually work with in the long term to ensure that ISIS and Al-Qaeda don't return. That's sort of a precondition and what we're saying is the degradation of that opposition through Russian airstrikes and through Syrian regime advances.

I think the most important question that all U.S. policymakers need to be asking themselves, and anyone who's sort of watching along and has an interest in the region needs to be asking is, who is the force that will come after ISIS? Is it going to be Al-Qaeda or is it going to be a non-Salafist opposition, and if the latter, what are we doing to protect that opposition?

John DeClue: Interesting. Well thank you Harleen. Really, I can't thank you enough for taking time to speak with us today. This is, I think, the third call that ISW has done with us to help our clients and prospective clients better understand the situation, and we as well, and I can't thank you and ISW enough for your support.

Instability in the Middle East continues to have one very negative spillover effect and that's its impact on the willingness of investors to take risk in a general and broad sense. And that, of course, can have a depressing effect on investment markets, whatever the source of that unease is. And certainly because of the potential for the Middle East to continue to create uncertainty, we watch the situation there very, very closely, and hence this call today.

So again, as I wrap it up, I want to thank you very much for your relationship with U.S. Bank and for taking the time to attend the call today. And as always, please contact your U.S. Bank advisor if you'd like more information on these and other timely topics. Goodbye.

Closing: Thank you for listening. We invite you to join us for future calls. Details can be obtained from your U.S. Bank representative.

Website: reserve.usbank.com



The information provided by Harleen Gambhir reflects her views and opinions and those of ISW. The information shared by John De Clue represents the opinion of U.S. Bank Wealth Management and does not constitute investment advice and is issued without regard to specific investment objectives or the financial situation of any particular individual. Since economic and market conditions change frequently, there can be no assurance that the trends described will continue or that the forecasts will come to pass. These views will be valid as of the date presented and are subject to change at any time based upon market or other conditions. The information presented is for discussion purposes only and is not intended to serve as a recommendation or solicitation for the purchase or sale of any type of security. Data, research and other factual information and statistics have been gathered from a variety of sources believed to be reliable but are not guaranteed as to accuracy or completeness. ISW and any other organizations mentioned are not affiliates of or associated with U.S. Bank in any way.