Impact of September 11, 2001 terrorist attack On Pakistan economy.

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DEDICATION

I dedicate this humble effort to my loving parents without whom I would have been nothing, to my teachers whose guidance, strength of character and spiritual learning showed me the dark moments of life. Due to their efforts I am able to complete this thesis.

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“In the name of Allah, the most compassionate, the most merciful”

Innumerable gracefulness to almighty Allah who is master of all universe .He who created time, space and knowledge and everything within the limits of these and beyond the limit of these. My deepest appreciation to all mighty Allah the most gracious and the most merciful. He provides me the health, opportunity, time, patience, courage, integrity, and ability to complete this task.

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Chapter 1

INTRODUCTION

Broad problem area/background:

Pakistan's economy has been on the downfall for the past several years, has been hit by poor crops, political chaos, social instability, corruption and sanctions in the past three decades. Pakistan’s economy has seen significant progress in fiscal year 2000-01 and afterwards. The year have seen Pakistan successfully restoring relations with the international community, acquiring high credibility for its reforms program, harnessing important resources at home and abroad, and putting into motion a broad participative process towards the revival of the economy. Given the difficult past that Pakistan’s macroeconomic environment had reached by the end of the last decade, the Government confined its stabilization and structural reform programs during the period. These include comprehensive tax reforms, trade and tariff measures, and price deregulation across important sectors, such as energy and agriculture, privatization of major public sector corporations, financial and capital market reforms, measures towards improving governance, fiscal transparency, and dedicated poverty alleviation programs.

Stabilization and structural reforms undertaken during the period have paid rich dividends. Sharp reduction in fiscal and current account deficits, an impressive recovery in industrial production, reasonable increase in tax collection, lower than targeted inflation, sharp increase

in credit to private sector, a modest growth in exports and remittances, and impressive build up of foreign exchange reserves have been the major success of last year.

Having achieved a major success on stabilization front, the challenges for the medium-term have been to rekindle growth through greater private sector participation and efficient public sector investment, thereby increasing employment opportunities and reducing poverty; in addition to achieving fiscal discipline so that the country's debt burden do not increase. It is in this background that a medium-term macroeconomic framework was prepared covering the period from 2001-02 to 2003-04 , the salient features of which include: taking the economy at higher growth path (5.2 percent- 5.5 percent) while keeping inflation at about 5.0 percent; fiscal deficit to decline further to 3.2 percent of GDP and current account deficit to decline to 1.3 percent of GDP; social sector spending will continue to receive highest priority; and foreign exchange reserves to reach slightly above $13.0 billion by 2003-04. It is believed that by the end of the medium-term program Pakistan will regain its lost growth momentum and macroeconomic stability on a sustained basis.

On the one hand September 11, 2001 terrorist attacks on the United States also have negative effects. Multinational companies, big buying houses and shipping lines have scaled down their operations because of uncertainty of war. Pakistan's defense budget, already straining the economy to a near breaking point, and on increase. On the other hand, Pakistan's support to the US in the offensive against Afghanistan has resulted in economic benefits from the US and other countries but also from financial institutions such as, the International

Monetary Fund and the World Bank. The US sanctions have been waived off and various financial aid packages including fresh loans, rescheduling of debt payments and wider access to international markets have been announced.

The fiscal year (2001-02) is the first year of the medium-term program. While fixing the targets of Pakistan’s key macroeconomic indicators for the current fiscal year the impact of possible slow down in global economy in general and the US economy in particular was taken into account. However, the unprecedented events of September 11 in the Untied States have unleashed new and unpredictable forces that have substantially raised the risk of global downturn. Developing countries were expecting a sharp downturn in their economic growth rates. Growth in international trade in 2001 may undergo one of the severest deceleration in modern times. The global economy entered the last quarter of 2001 with unsteadily balance between recession and recovery. Pakistan, being the part of the global economy, was not expected to remain unaffected due to these developments.

Statement of the problem:

In this backdrop the study is prepared to answer the following questions.

1. What was the impact of September 11, 2001 terrorist attacks on the United States on G.D.P of Pakistan.
2. What was the impact of September 11, 2001 terrorist attacks on the United States on Inflation of Pakistan.
3. What was the impact of September 11, 2001 terrorist attacks on the United States on Fiscal deficit of Pakistan.
4. What was the impact of September 11, 2001 terrorist attacks on the United States on Exports of Pakistan.
5. What was the impact of September 11, 2001 terrorist attacks on the United States on Imports of Pakistan.
6. What was the impact of September 11, 2001 terrorist attacks on the United States on Defense Budget of Pakistan.

Significance of the study:

The World Trade Center incident was the most devastating incident to have occurred in the world. Not only was it an act of terrorism that shook the entire world, but it occurred in the world's biggest economy, that is an economic pivot for the entire world. The USA is today one of the most developed nations in the world. The exports of many third world countries and virtually the entire economies of these countries are dependent on the economic well being of the USA.Since Pakistan is a third world country whose economy depends on a large part on the export/import trade and the aid provided by well-developed countries, foremost among these the USA, so conducting research on the economic effects of this incident is very critical at this point in time.

The other reason for conducting research is to see how the concept of globalization is quickly eradicating national boundaries and making the whole world a global market.Far better to judge it critically on the extent to which it advances our highest aspirations such as peace, freedom, and broadly shared prosperity. September 11, 2001 terrorist attacks on the United States puts at risk many of the gains globalization has brought, but it likewise may present opportunities to smooth some of the rough edges of the globalization associated with American policies of the past decade.

To skip to the punch line, the future trajectory of globalization is not preordained; it lies largely in our own hands. The fact that the occurrence of an incident on the other side of the world can directly impact the Pakistan economy is a case in point. The strategic location of Pakistan and its vicinity to Afghanistan is another reason why this incident directly affected the Pakistani economy. Also the economic volatility of this country is an important point to bear in mind while conducting this research.

The fact that this study is exploratory as well as a hypothesis and one also proved a challenge due to recency of this event and also because there has been limited previous research in this field. The significance of this study is all-evident from above reasons. I have chosen the main and important factors that have been effected by September 11, 2001 terrorist attacks on the United States. In the research I have come to known that what and how they are affected.

Scope and limitations of the study:

Scope:

The researcher has a diverse scope in this project. Seven main factors were selected which were affected by the September 11, 2001 terrorist attacks on the United States. Due to globalization, an event that occurred in United States of America can have deep-rooted impacts on the economies of other countries, especially those of third world countries that are highly dependant on developed countries for financial assistants as well as international trade.

The factors selected were, inflation, fiscal deficit, imports, exports, GDP and Defense Budget. These factors have a major impact on Pakistan economy with the relation of September 11, 2001 terrorist attacks on the United States. They are the major sources playing part in the up rise or downfall in the Pakistan economy. That’s why these factors were selected.

Limitations:

1) Time constraints:

This project had to be completed in six months and the researcher was bound in this time frame for the collection, analysis & interpretation of the data.

2) Use of only secondary data:

The project entailed the use of secondary information. Hence there was no need for a questionnaire or any surveys or interviews were necessary.

Definition of terms:

Financial Markets:

Financial Markets are all institutions and procedures for bringing buyers and sellers of financial instrument together.

Capital market:

It is the market for relatively long-term (greater than one year original maturity) financial instruments (for example bonds and stocks).

Commercial Bank:

It is a dealer in credit or more properly a dealer in money. It is an intermediate party between the borrowers and the lender. It borrows from one party and lends to another. The difference between the terms on which it borrows and is on which it lends forms the source of its profit.

Recession:

A sustained drop in the level of economic activity.

Gross Domestic Product (GDP):

The value or total output actually produced in the domestic economy over a period of time (usually a year).

Globalization:

The process by which most economies around the world have become most interdependent. The term is applied especially to the increased integration of financial markets that has occurs over the last three decades as a result of reducing regulatory barriers to international financial flows.

Federal Reserve Bank:

It is the central Bank of USA. It is one of the twelve banks each operating in a different area of the US under the authority of the Federal Reserve System.

Chapter 2

Literature review

Natural or man-made disasters have always had an enormous impact on global economies. Great depression, 2nd World War, 1995 Kobe earth quake, Gulf war, 1998 Pak nuclear explosions and the recent 11th September attacks on world trade center (WTC) have all had effects of different magnitudes on the economies in their respective regions and those who depends or have any link with those regions.

On the global level 2nd World War, The Great Depression and the WTC incident have all played havoc with the global economy and have further pushed the economy in recession. The WTC incident is however the most devastating event since the 2nd World War, we are not mentioning the Gulf War here as its affects were micro in nature and their affects were not only confined to the Gulf region but also their impact on our economy was not much.

The Great Depression:

The Great Depression of 1929 was one of the worst depressions the world has ever seen. The stock market collapsed and was in shambles, banks every where went under, a quarter of the work force about 13 million people were unemployed in 1930.When Dollar inflated, the prices of real estate and stocks sky-rocketed, this led to the

ultimate crash of the stock market on 29th Oct, 1929 (Mike Noble, 2000).

Credit expansion and inflation artificially reduced the interest rates thus sending false signals to businessmen. More money leads to an economic boom, which causes prices to increase. Each time prices increase for capital goods, used for business expansion, the costs of doing business increases. The prices continue to swell until businesses can't afford to remain in operation. These and other policies pursued by Cal Coolidge made the stock market crash inevitable and depression inescapable.

World War 2:

World War II might possibly be the most influential event in America's history. The War's effects can be seen throughout all aspects of our lives today, from the technology of cellular phones, to the increasing number of women in historically male dominated careers, such as aerospace engineering. Regardless of our view on World War II, it is indisputable that it has had a profound and lasting effect on the United States and the rest of the world as well.

At the beginning of the war, there was an instant need for both soldiers and money. A draft provided American government to sell war bonds to willing entrepreneurs. Another draft enabled Govt to recruit as many soldiers as needed. These two measures were only transitory as the

support for the war filled the recruitment offices and war industry began.

War industry was probably the biggest part of the war that aided the United States progress into the twenty-first century. War industry came in many forms, from companies switching production to brand new companies being formed to supply the awesome demand of the war. Immense industrial buildings were built to make, bombs, airplanes, weapons, and clothes for the soldiers. New companies and converting companies received commissions from the government to fulfill in order to help the war. The government not only bought all the goods that were being created, but also financed the beginnings of new companies, and new technologies. American companies such as Ford, General Motors and Chrysler all switched their car assembly lines into virtual war machines. The plants would mass-produce everything from bullets to tanks to airplane engines, the cost of conversion, amply covered by the commissions of the federal government. As effective as the older companies, were new companies commissioned to build the new tool of destruction that World War II is famous for, the airplane. Companies such as McDonalds, Douglas, North American Aviation, Cadillac, Dodge, Boeing and Lockheed answered the government's call to be producing over 125 thousand airplanes by 1943. By numbers, the USA federal budget increased during the war years by $91 billion dollars, to $100 billion.

I998 Nuclear Explosions:

Pakistan's detonation of nuclear devices in May 1998 resulted in the imposition of sanctions by America and other aid giving countries. According to the fact sheet released by US state department, Bureau of Economics and agricultural affairs, on 18th June 1998, United States;

"Terminated or suspended foreign assistance under the FAA with humanitarian exceptions provided by law. Terminated foreign military sales under the Arms Export Control Act and revoked license for commercial sale of any item on the US munitions list. Issued executive orders to prohibit US banks from extending loans to the governments of India and Pakistan. Gained G-8 support to postpone consideration of non-basic human needs for both the countries".

In case of Pakistan the loss of US bilateral assistance did not have a very significant affect following May 1998 tests because Pakistan was already under US sanctions imposed by the 1985 Pressler amendment.

In total fourteen countries including Japan, Australia, Canada, Germany, Denmark and Sweden suspended bilateral aid programs against both the nations. Among these however only the Japanese sanctions involved significant amounts. Japan suspended all loans to Pakistan that totaled $ 231 million in 1997-98 and cancelled grant aid of approximately $ 55 million. Although Australia did not cancel its aid to Pakistan as all of it was classified as humanitarian but it refrained from a planned increase of $ 2.5 million.

In November 1998, the Clinton administration eased some economic sanctions against Pakistan. These waivers were given because trade and development organization and overseas private investment co-operation and department of agriculture concluded that if new business was closed with India a projected $ 3.5 billion loss would be incurred by US exports. This was in addition to $ 300 million in OPIC guarantees to Pakistan and $ 500 million in Exim Bank. Though Exim Bank's exposure to Pakistan was $ 429 million.

Terrorist Attack of 11TH September:

11th September, Tuesday, 2001 seemed very much like any ordinary day in the busy Manhattan streets of New York, yet in a while something was going to happen that would irrevocably change the entire geo-political situation/scenario in the world. At precisely 8:35 am a time when people were getting their work started United Airliner crashed into the North tower of the World Trade Center, symbol of American power, minutes later another airliner crashed into the south tower. The world was astounded as the symbols of American superiority were reduced to mere rubble on setting the threat of a global recession. These attacks set of a chain reaction of events which had great economic ramifications for the entire world.

Impact on America:

An economist once very aptly remarked that

“When American economy sneezes, the rest of the world catches cold”.

How very true seems that the world was waiting for an incident like this to be tilted into recession. Tuesday’s attacks have left an indelible mark on the economy and global culture; these attacks not only affected America but also had great impact on our economy.

Economists say that a global economic contraction is almost certain as world stock markets plunged, US dollar spiraled lower against the Yen and Euro and oil/gold prices soared after the terror attacks in New York. For years US has been seen by investors as a safe haven, offering returns better than those available in Europe and elsewhere. Analysts speculated that these catastrophic events could deal a hammer blow to US confidence and could send already wary investors fleeing to gold and other assets (Paul O Neill, 2001).

Markets remained shut across US, which attracts almost 2/3 of all the global capital inflows, in the wake of the terrorist attacks were to remain closed till Wednesday. The closure of markets marked the only second time the New York stock exchange has remained close for two consecutive days, the last being to honor the World War 2 August 1945.

All this added ambiguity as to how investors would react to the tragedy. A full blown global recession was likely says Sng won sohn, chief economist at Wells Fargo and Co. Recently, the economy has been on a high wire act, straddling between recession and anemic growth, thus damage

to confidence will further push USA into recession. Major risk once the stock markets reopen panic in the financial markets which will result in large movement of capital triggering a global recession.

Kevin Logan, an economist at Dresdner, Kelvin Wort Wasserstein summed up the feelings of many by saying 11th September events meant that business will not be as usual anymore [Paul O' Neill, 2001]

The September incident in USA has destroyed approximately US $ 13-$15 billion of private and government capital. It has pushed USA even more into a recession and resultantly has slowed the economies through out the world. The impact of the incidence has affected the airline, hotels and banking/insurance industries. In order to boost up the economy’s policy makers are to restore and bolster consumer confidence and demand by increasing liquidity to the global financial system (Dr Khalid -A- Mallick, 2001)

The three industries with the greatest job impacts are securities, retail trade and air industry (Consult Appendix-A). Businesses in the first two sectors are likely to suffer because they occupied substantial space in WTC and surrounding buildings. While several other industries in New York were immediately hit by adverse spill over effects. Air travel was the first affected, with peoples desire to travel by air plummeted (James Parrot, 2001)

Chapter 3

Research Methodology:

The research I have undertaken is descriptive in nature since the incident occurred four years before therefore there are some researches conducted on the issue as impact of September 11th attacks on global economy and one or two researches were made on Pakistan economy affected by September 11th attacks. This is not the first time I am collecting the data therefore it is secondary in nature.

Before I conducted the research there was very little information about the effect of September 11th attacks on the Pakistan economy. In addition, the incident was entirely unprecedented in nature, therefore not much was known about the situation at hand.

All the data conducted is secondary in nature, collected from Internet, economic survey of Pakistan, print media, newspaper articles and magazine. Extensive data was collected to understand the issue and get a handle on the situation. Although research has been conducted on a global level but I conducted to see the effects of these devastating attacks on the Pakistan economy.

The study is not purely exploratory since it was conducted with intention of proving that such incidents of disaster and terrorist incident can affect the economies of the effected countries as well as those dependent on it. Pakistan is highly predisposed and sensitive to any economic calamity occurring in a developed country.

Chapter 4

RESULTS & DISCUSSIONS

Short-term effects:

1) The destruction of life and property:

This includes the tragic loss of human life, the costs of replacing the buildings and equipment destroyed in the attack, and the disruption of activities in the immediate after-math of September 11. Also included are the somewhat longer-term disruptions to specific industries, most notably to the global airline industry and related services, such as hotels, local transportation, tourism, civilian aircraft manufacture, and restaurants, as well as the postal service in the wake of the anthrax scare in the United States.

2) The confidence channel:

An unexpected event of the magnitude of the September 11 attacks alters the assessment of economic risks by both consumers and businesses in a negative way. The resulting deterioration in confidence about the future can reduce the incentive to spend as opposed to save a process that can spread through the economy and the rest of the world through normal business cycle and trade channels.

3) Financial market responses:

By their nature, financial instruments involve commitments across time, and thus are affected by perceptions of the future. For example, equity and bond markets trade securities involving future dividend or coupon payments by corporations or governments. In addition, derivative markets can provide information about the level of uncertainty in traded markets, an issue of particular interest after such an unexpected event as the terrorist at-tack. The initial generalized fall in asset prices has now been reversed, although borrowing costs for riskier borrowers remains high.

4) Commodity markets:

Slowing activity will reduce the demand for commodities and other goods sold in similar markets, such as computer chips, while initial concerns that supply might also be disrupted (most notably in the oil market) have not thus far transpired. Commodity prices (particularly for oil) have weakened sharply, reducing the impact of fall in aggregate demand in industrial countries by transferring part of these losses to commodity producers through terms of trade.

Long-term effects:

The main channel through which the continual threat of terrorism could affect the long-term potential of the global economy is by raising transaction costs, resulting in a reduction in potential output. The costs can be broken down as follows:

1) Higher operating costs:

Businesses may experience higher operating costs, owing to increased spending on security, higher insurance premiums and longer wait time for activities.

2) Higher levels of inventories:

Businesses may be required to hold longer inventories than previously required, owing in part to less reliable air and rail transportation. There is anecdotal evidence from the auto industry that production was interrupted because components were not immediately available from suppliers after the September 11th attacks, owing to delays in shipments crossing the U.S.-Canada border.

3) Higher risk premium:

As a result of attacks lender appetite for risk declined, leading to higher risk premiums that may be passed on to business in terms of higher interest rates and lower equity prices.

4) Shift away from globalization:

The attack may have effects on firm's investment decisions. Whether to invest abroad because of potential disruption of cross-border flow of goods and services. Costs for such transactions may rise owing to closer inspection of transactions and higher insurance premiums (World Economic Outlook, 2001).

Item	1999-2000	2000-05
CPI (General)	3.6	4.4-
Food Group	2.2	3.6-
Non-Food Group	5.0	5.3-

Inflation:

Inflation, on the basis of Consumer Price Index (CPI), was 4.4 percent in 2000-01 as against 3.6 percent of last year. Food inflation was 3.6 percent and non-food inflation was 5.3 percent in 2000-01 as against 2.2 percent and 5.0 percent respectively in the preceding year. The main factor responsible for a relatively higher inflation in 2000-01 as compared with previous year has been the upward adjustment in product prices necessitated by the rise in their prices in international market. Despite several adjustments in POL product prices and about 18 percent depreciation of currency, inflation in Pakistan remained below the targeted level of 6.0 percent. Prudent fiscal management and tight monetary policy succeeded in maintaining price stability during the fiscal year 2000-01 as a part of the stabilization effort.

Table 1: Inflation

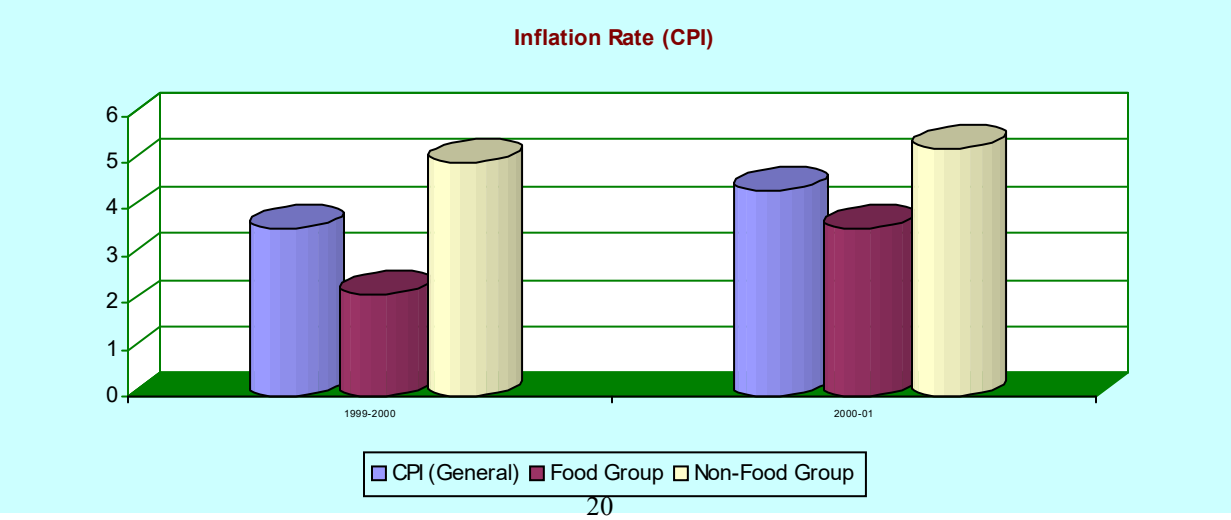


Table.2 Source: Federal Bureau of Statistics

One of the most significant achievements of 2000-01 has been the sharp reduction in overall fiscal deficit. Fiscal deficit as a percentage of GDP averaged 7.0 percent in the last two decades (1980s and 1990s). This has been the major cause of macroeconomic instability in the past, especially in the 1990s. Stabilization measures taken during 2000-01 succeeded in reducing the fiscal deficit from 6.5 percent in 1999-2000 to 5.2 percent in 2000-01. CBR revenue during 2000-01 amounted to Rs 393.9 billion as against Rs 347 billion last year, thereby registering an increase of 13.5 percent. This has been the second consecutive year when tax collection increased by more than 13 percent. Direct tax increased by 12.8 percent while indirect tax registered a growth of 13.8 percent. Within indirect tax, sales tax grew by 30.9 percent and custom duty increased by 4.6 percent.

Impacts on the Defense Budget

The centrality of the Pakistani armed forces since independence resulted in higher allocation to defense. This trend continued.

Fiscal year	Defense Expenditure (Rs million)
1996-97	127,441
1997-98	136,164
1998-99	143,471
1999-2000	150,390
2000-2001 (M.B.E)	157,500
2001-2005	210,000

M.B.E-Modified Budget Estimates

Source: Pakistan Economic Survey 2000-2005 at, <http://www.finance.gov.pk/survey>

Even though Pakistan's fragile economy has been unable to support the high defense expenditure, the military spending in Pakistan has been at the cost of development expenditure. An additional factor, post-September 11, straining the Pakistan economy is the increase in the defense budget. It has been reported that the government is expecting significant increase in its defense and law enforcement budgets due to the developments taking place after September 11.The Finance division in fact states that balance of payments and the budget 2001-2002 were likely to be affected. The unwanted developments will negatively impact the current account deficit situation by raising the overall financing requirements of the military government.

Estimated Cost of War

It is difficult to assess, and it is too early to tell, what will be the medium term impact of Pakistan's front-line status in the US war on terrorism on Pakistan's economy. Some observers have assessed that the immediate and short-term impact would vary between $1.5 billion to $2.5 billion during the current financial year. This is in addition to the non-quantified adverse impact on foreign investment and also the national output.

Positive Moves for the Economy Post-September 11

After Pakistan's support to the United States war against terrorism some of the economic aid suspended earlier was resumed. Not only are the US and other nations offering economic benefits but also financial institutions like the International Monetary Fund and the World Bank and the Asian Development Bank are coming up with financial support packages to Pakistan.

Economic Packages for Pakistan

Agency/Country Amount assured/Committed Remarks World Bank$300 million. The loan is to help privatize and restructure the banking structure. The loan was on schedule for lending to Pakistan before the September 11 attacks in the USA. Also, dialogue for some additional funds is on between the two parties, figures for which are not disclosed. International monetary Fund Special Drawing Rights (SDR) 1.304 billion (about $1.322 billion). The Executive Board of IMF has approved three-year arrangements for Pakistan, totaling Special Drawing Right (SDR) 1.034 billion (about US$1.322 billion). As a result of this decision by IMF Pakistan will be able to draw SDR 86.16 million (about US$109.6 million) under the arrangement. Asian Development Bank$950 million (for the year ending December 31, 2001) this is a substantial rise from ending $626 million planned before the events of September 11. United States of America $1 billion (approx) Two installments of $50 million in grant America have been released. The US has already rescheduled Pakistan's repayment of $379 million for the year 2001. In terms of direct assistance there is $95 million in ongoing programmer of assistance, in democracy, education, heath, child labor elimination and counter-narcotics. The US will also provide $30 million in food assistance over the next year and $73 million for border security and law enforcement programmed. In addition to all this, there is the Export-Import Bank (EXIM) money, as much as $400 million, and Overseas Private Investment Council (OPIC) money as well, of $200 million.Japan-Rescheduled repayment of their dues of US$550 million. Canada-Rescheduled

repayments of their dues of US$238 million. Also, $300 million loan has been converted into a development funding. Britain$152 million it is a three year loan. United Arab Emirates$265 million financial assistance is for four different hydropower projects.

Affected Sectors:

Although a number of industries were affected by the attacks but we took four sectors which we thought were linked to the attacks.

These four sectors are important as till 9/11, our main imports were as follows: petroleum products $148.254 million, textile machinery $33.148 million and main exports were cotton yarn and garments 82.97 and 82.07 million (Dawn).

Fuel and Energy:

Mari Gas and Hub Power were both affected by the attacks. Hub Power companies which fell down Rs 1.20 at Rs.14.60 on 29 million shares. While Mari Gas fell down from $ 22.15 closing to $21.70 on 13th September.

Oil prices have been caught in a two-way pull since the devastating attacks on US targets on Tuesday. Concerns that US retaliation could draw the Gulf-Arab producer nations into a wider conflict have been pulling against concerns about the impact of crude demand on the assault on the hub of global capitalism. There are also concerns that the Arab oil producing countries could turn to oil weapon in the face of any US-retaliation. Traders have not forgotten the surges of 1973-4, 1990 and last autumn that followed a

stand off between Western powers and Arab crude oil producers.

In this current upheaval the organization of Petroleum Exporting countries (OPEC) has promised to pump enough oil to world markets to ensure their stability after the attacks. (Dawn, 15th Sept 2001).

Impact on the Airline Industry:

The recent terrorist attack added pain to the already injured airline industry in 2001.There was total panic in the airline industry at the highest levels. In America, the immediate grounding of all flights bled about $ 650 million from the industry with a projected loss of $ 3 billion this year. United and American Airlines each announced the elimination of 2000 jobs. The US government offered the airlines cash grants, loan guarantees and tax cuts worth $ 5 billion and an additional $ 3 billion to pay for increased security (though they had requested $ 24 billion). European airlines estimated a loss of 775 million Euros ($ 713 million) compared with a previous forecast of net profit of 645 million Euros. Implicitly, the impact on airline industry had a ripple effect on the tourism industry in many parts of the world. Ref (Rogate Mshana 25 February 2002).

Insurance industry:

The industry is affected by large claims resulting from the attacks, but gain from sensitive uncertainty and interest in security. Subjective evidence largely from the United States indicated that insurers have been able to raise premiums, while it remains unclear how far governments was involved in covering losses from terrorism

and war. The market assessment is that the benefits of higher premiums will dominate, as relative equity prices for insurance brokers have risen by around 10 percent in the United States.

Other services industries:

Other services industries have been badly affected, such as hotels, tourism, car hire travel agents, restaurants and civilian aircraft manufacturers, while postal use fell after anthrax scares. For example hotels have reported higher vacancy rates. And employment in the sector as a whole in the United Stated fell by 58000 about 3 percent in October and November. Tourism has been particularly affected in regions of the world dependent on foreign visitors. Such as the Caribbean, parts of the Middle East, and portions of Asia. Relative equity values for hotels and leisure facilities are off by around 15 percent in the United States and Europe, although they have gained slightly in Japan, possibly reflecting the more limited need for air travel.

Impact on Pakistan:

The 34 days that followed Sept 11th unleashed a wave of shock for Pakistani business and industry. Pakistan’s economy is said to have suffered a loss of one billion dollars over the last one month after the attacks, will need debt relief, trade concessions and grants in order to overcome it’s problems (The News, 15-10-01).

The government thinks that the Western largess will take us out of this quagmire but the picture is not as rosy

as is being painted. The latest estimate of Pakistan's export losses now are projected at $ 3 billion --- that is a hefty third of the annual exports. Increased shipping and air cargo's cost and newly war surcharge. The opponents of Islamabad's co-operation with Washington point to the meager emergency economic assistance, totaling around $ 150 million that has been promised so far by US, Japan and European Union. In the Bush versus Osama war, the first casualty was Pakistani foreign trade.

Increased shipping and air cargo cost and newly imposed war risk insurance may cost $ 75 - $ 100 million than usual. Following Sept 11th, the industry and business are forced to pay an additional $ 460 per container on foreign trade to and from Pakistan on account of War Risk Insurance (WRI), cargo insurance and freight rate increase. Foreign buyers have almost stopped placing new orders also because of the negative projection of Pakistan by World Media. It shows big anti-US protest and portrays that it may disrupt production and non-fulfillment of export orders.

Pakistan a relatively weaker economy was almost devastated by the 11th Sept attacks. Stocks on 11th Sept virtually crashed on panic selling originating from all the quarters owing to turmoil in the world's major financial and trading centers following reports of devastation in the US.

The KSE 100 share index fell by 4% or 48% points at 1208.30 as fears of US missile attack on Afghanistan gripped the market and leading base shares fell like nine pins. There was a panic all around as the leading bulls saw helplessly the KSE index falling like house of cards under

the weight of mounting selling offers but no willing buyers. The KSE index finally ended lower by 47.69 points or at 1208.30, signaling that it would break through the 1200 point’s psychological barrier in the next few days. The market capitalization fell by 10 billion at Rs 306 billion (Consult Appendix-B).

The intensity of panic selling may well be from the fact that everyone is in a haste to get out of the market almost whispers of further price erosions. However a section of leading investors did not join those what got panicky without having an objective view of the entire scenario awaited the end of the panic, which n e broader context may have no relevance to the Pakistani situation, claimed a member of KSE (Intesham-ul-Haq, Sept 2001)

Pakistan's entry into the international coalition against terrorism and its becoming a front line stage state in that context has enhanced risks to the economy. Despite an unexpected increase in foreign financial assistance and freer access to the US and the European Union on account of higher freight, war risk insurance and fewer buyers are going to conversely affect the economy. (SBP, s annual report, 2000-01) (Dawn-31stDec, 2001).

Masood Naqi, chairman of textile and exporters association sounded more pessimistic, we may see a 50% reduction in exports. Major airlines have cancelled their cargo and passenger services to and from Pakistan, directly damaging exports. Foreign buyers no longer visit Pakistan to place orders. Costs of imports and improved raw materials inputs have gone up. As the political situation in the region becomes murkier with each passing day and the nearby Gulf region is being looked as a war zone by many

foreign investors of Pakistan, financial analysts predict rupee losing 6 - 8 % against the dollar in the next ten to twelve weeks.

Businessmen are of the view that an economic downslide in Pakistan was evident for more than a year. ‘Drought’ was then the ready made excuse available to the financial managers. Now it is the fast changing scenario from Atlantic to Indian Ocean and the sequence of events which has pushed Pakistan again as the front line state, which is a convenient excuse to cover up all that could not be achieved.

He pointed out the year 2000-1 ended with the lowest growth rate in the history at 2.5 % (a senior businessman remarked. Before these fatal attacks attracted $ 287 million as foreign direct investment. Textile $ 4.5 million, oil exploration attracted $ 73.1 million, petro-chemical and refining $ 8.6 million, tourism $ 1.4 million. This investment is expected to fall drastically as a result of these terrorist attacks (Consult Appendix-C).

Financing Terrorism:

The so-called `war against terrorism' has brought into existence a new global policy initiative to stop the flow of financial resources to terrorist organizations. This move, it is argued, may affect the composition of financial flows in and out of developing countries. This is because ordinary residents of these countries, as well as terrorists, use informal and sometimes illegal mechanisms for transferring funds. The new policies are expected to shift more transactions to legal and traceable channels

(and thus taxable). This might have a dampening effect on their volume.

Security Council adopted Resolution 1373, which requires that all member states prevent and suppress the financing of terrorism. The UN, the Financial Action Task Force on Money Laundering (FATF), the IMF's Financial Sector Assessment Program (FSAP), and the finance ministers and central governors of the Group of 20have combined efforts to fight cross-border money laundering and terrorist financing. The International Monetary and Financial Committee (IMFC) called on all countries to set up Financial Intelligence Units (FIUs) to fight money laundering by 1 February 2002 2. The formal banking systems and non-bank financial institutions that are used for commercial transactions may also be used as channels for terrorist-related transfers. (Garry J. Schinasi, Chief of the Emerging Market Studies Division in the IMF Research Department, IMF Survey, 30 July 2001)

Effected sectors:

Impact on Trade:

Soon after September 11, 2001, when the US President George W Bush issued threats and warnings to wage a war against terrorists by attacking Afghanistan, media hype regarding uncertainty of war began to grow. This generated fear in the Pakistani market, and so immediately after September 11, many multinational companies, airlines, shipping lines and big buying houses cut down their operations in Pakistan.

This clearly gets reflected in President Musharraf's statements that "one of the major concerns for the country was that foreigners working in different projects were leaving Pakistan" and "a number of orders that were placed with our industries have been cancelled and no fresh orders were being placed".

Like many of the developing economies, textile exports constitute the backbone of Pakistan's export strategy. This particular sector seems to have been badly hit following the September 11 developments. The Chairman, Pakistan Readymade Garments Manufacturers and Exporters Association Masood Naqi said that textile exports comprise around 65 per cent of US$9 billion total exports and because of the steep fall in new orders, there would be loss of around $2.5 to $3 billion in export earnings. September onwards is the time when a large part of commercial activity takes place in the Pakistani textile industry. This is mainly due to the fact that the fresh cotton crops unveil themselves and the traders in Pakistan start receiving Christmas orders from their clients in the US, Europe and the Far

East. The impact of these cancellations of orders in the fabric and knitwear industry will be felt in revenue and foreign exchange earnings in due course of time but the negative signs of this are already affecting the vendors, daily wage earners and the small industry.

Media reports suggested that not only cancellation of orders was hitting the Pakistani market but also a number of foreign airlines have either closed down their flights to and from Pakistan entirely or partially. Due to this Pakistan's trade has been badly hit. Insurance companies have added war risk charges on all trade to and from Pakistan's shipping ports. Though insurance companies have levied war risk charges on the whole region, for Pakistan these charges are the highest in the world. All these factors made Pakistani products uncompetitive in the international markets. Estimating the losses the Commerce Ministry opined that "exports could decline by $1.4 billion this year as buyers are reluctant to book new orders and some of them have cancelled the old orders. Private sector fears that the loss of exports may be as high as two billion dollars this year."

Pakistan's travel and hotel industry have been badly affected. The fall out of the developments after September 11 brought down the business by approximately 80 per cent during the period September 2001 to January 2002. Due to this more than 30,000 employees have been laid off. Along with this, the airline industry also suffered major set back. PIA (Pakistan International Airlines) has suffered a big loss. PIA estimated a profit of Rs 130 million for the period of September 2001. But contrary to this, the airline suffered a loss of Rs 300 million in October. It is

expected that a large number of workforce in this area would also be laid off.

Banking sector:

Bank: - Data as of end 2001 (in Billions of Rupees)

Institution	Bank Deposits	Bank Advances	Investments	Total Assets	Bank Branches
NCBs	468.2	261.8	172.8	655.1	4772
Privatized Banks	204.0	93.1	86.8	246.0	2201
Specialized Banks	16.1	98.0	5.6	138.1	534
Private Sector Banks	151.6	77.3	60.9	255.3	542
Total	839.9	530.2	326.1	1294.3	8049
FOREIGN BANKS	231.8	113.9	75.9	293.2	81
GRAND TOTAL	1071.7	644.1	402.1	1587.6	8130

The average return on equity (ROE) from 1990-98 for foreign banks was 23% p.a. and 20% p.a. for private local banks. However, during 2000 & 2001 sector ROE reduced considerably due to a downturn in the economy. Historically, spreads have remained between 5-6% until 1998. These have come down to about 4% in 2000 primarily due to the economic pressures. (State bank annual report).

Textile:

The next few years will determine whether the Pakistani textile industry can shape itself up and grab the opportunities offered, especially at the present moment when quotas are being enhanced and the tariffs are being reduced in many countries, as a concession to the Pakistan's help against terrorism.

The Pakistani textile industry is planning to enhance the textile sector's share in GDP from 7.5 percent to 9 percent and exports from the present $5.5 billion to $14 billion in the next four years. The plan envisages modernization, balancing and expansion on a large scale. The industry will encounter several problems at different levels. The textile industry in Pakistan is a capital intensive as well as labor-intensive industry.

Due to several reasons, the textile machinery manufacturers have been reduced in number significantly. Few bigger groups have emerged which have more or less a monopoly in sophisticated equipment. The competition is, therefore reduced and prices being asked for the new technology and equipment are enormous.

Unfortunately, Pakistan has no machinery making capacity worth the name, whereas our main future competitors, India and China, have huge capacities in this field. The cost of equipment of their textile industry will be much less than ours because we are dependent on imports. This will certainly put our expansion program at a disadvantage and will increase our cost of production; however, this

disadvantage can not be over come even if we start building our own manufacturing capacity right away. So in the next few years, we have to live with the fact that the machinery will have to be imported and at a cost, more than our competitors. (Business recorder)

Structural Reform Measures

Stabilization alone does not necessarily guarantee growth. Therefore, as stated earlier, stabilization program was supported by a series of wide-ranging structural reform measures needed to enhance economic incentives and improve resource allocation, as well as to remove obstacles to private sector development. One of the most important reforms launched by the government is the tax reform with a view to broadening the tax base, minimizing tax evasion, restructuring the tax administration, listening to the grievances of the tax payers, improving refund process, and documenting the economy. The critical area of tax reform, so far undertaken, entailed a drive to tax survey and documentation of the economy, the introduction of a two-tier agricultural income-tax, a reduction in number of federal and provincial taxes, the establishment of an office of the Tax Ombudsman, and the broadening and streamlining of the GST. The results so far have been encouraging. For the second consecutive year, Pakistan has had double-digit growth in tax collection.

In the areas of de-regulation and privatization, a privatization law has been enacted and expressions of interest have been received for major transactions in the oil and gas, energy, telecommunications, and financial

services. A petroleum price adjustment mechanism has also been introduced, while furnace oil was excluded from the freight pool, LPG was deregulated, and the Gas Regulatory Authority was established. Market-based agricultural pricing policies were put in place and the government is gradually reducing subsidies in agriculture.

Under financial sector reform, the regulatory role of the State Bank of Pakistan (SBP) was strengthened and the Banking Companies Ordinance to enforce capital adequacy ratio in line with international standards was amended. The Security and Exchange Commission has also been further empowered whilst the insurance sector has been de-regulated. Management of the Nationalized Commercial Banks (NCBs) was changed to introduce greater professionalism and autonomy in their operations. The CIRC came into operation to look into the issues of non-performing loans, and profit rates on national savings schemes (NSS) instruments were rationalized. The three large NCBs have been encouraged to trim their top-heavy structures to prepare for privatization. Substantial downsizing have already taken place in these NCBs.

A lot of stress has been placed on improving governance and deep-cutting civil service reforms have been initiated. The Federal Public Service Commission has been granted a greater degree of autonomy, with a strong focus on the training and improved procedures for performance assessment of civil servants. Pay and Pensions reforms have also been completed, while reforms in the field of public accountability, devolution of power to the district level, and better delivery of services by the government have been undertaken. In the area of fiscal transparency, audit and accounts have been separated, adhoc public accounts

committees have been set up at the federal and provincial levels and a new system of financial controls and budgeting has been established. Fiscal data are now regularly published monthly on the website of the Ministry of Finance and a fiscal reform unit has been established at the Ministry.

The government has taken a conscious decision to bring the issue of poverty alleviation to centre-stage in the formulation of economic policy. To this end, a strategy to reduce poverty and improve income distribution has been put into place. The strategy is based on the premise that sustained economic growth accompanied by macroeconomic stability is the most powerful means of reducing poverty in the medium-term. Although, growth is absolutely essential, focus on this alone will not be sufficient to achieve poverty alleviation, for which direct poverty reductions programs were required. It is with this in view that the government launched a rural-urban small public works program (Khushal Pakistan Program), the Zakat and Ushr system have been revamped, micro-credit (Khushali) Bank has been established, and a food support program has been launched to benefit the country’s poorest households.

Chapter 5

Conclusion

The study is exploratory since it was conducted with intention of proving that such incidents of disaster and terrorist incident can affect the economies of the effected countries as well as those dependent on it. Since Pakistan usually depends on USA aid and direct foreign investment so Pakistan is highly predisposed and sensitive to any economic calamity occurring in a developing country. So the events like terrorist attack on WTC are likely to affect the global economy due to globalization, and because the world becoming a global village.

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This is to certify that, Sheraz Khattak of BBA.6 (E) has completed the final thesis report on" **Impact of September 11, 2001 terrorist attack On Pakistan economy"** under my supervision**.** By Friday, February 09, 2006.

Project supervisor