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Terrorist Attacks in New York City and Washington, D.C.: Implications for the U.S. Economic Outlook[1]

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This paper is one in a series prepared by faculty in the Department of Food and Resource Economics at the University of Florida. Other papers in the series address implications for U.S. trade policy (FE 312); state government revenues in Florida (FE 317); and the Florida citrus (FE 313), vegetable (FE 314), agronomic crops (FE 315), and tourism (FE 316) industries.

The terrorist attacks did not cause any substantial economic change. Terrible though they were, they only accentuated underlying trends that were already taking place. We were already in a recession, albeit not admitted. People were cutting back on big ticket items, luxury spending, and travel before the attacks. Markets suffer in recessions, but despite the week's fall of around 14 percent to the low 8,200s, on September 21st, the Dow Jones Industrial Average was trending downwards from 11,350 in mid-May. This is mainly because company operating profits per share were falling faster than at any time since the late 1960s. The index of leading economic indicators fell 0.3 percent in August when economists had forecast a drop of 0.1 percent. The Conference Board Consumer Confidence Index was also trending down. In September 2000, it was around 140; in August 2001, it had fallen to 114; and by September, it had fallen to 97.6, the biggest one month fall since October 1990. The index is reinforced by the University of Michigan's Consumer Sentiment Survey with an annual decline from 108 to 84. The Federal Reserve cut the federal funds rate for the eighth time this year. International investment was already the worst in 30 years, down from $1.3 trillion to $790 billion. The state of Florida's budget was already in trouble. All these were existing trends.

There is, however, no doubt that the attacks have accentuated the existing consumer reluctance to spend. One money manager was quoted as saying, "In terms of psychological depression, I don't think there has been anything equal to this." Since September 11th, the market has lost about $1.4 trillion, about the same as Great Britain's annual output. Historically, a sustained $1 increase in stock market wealth adds some $0.03 to $0.05 to consumer spending and a $1 fall has the opposite effect. Consumer confidence to spend and businesses to invest have both been hurt. Sales at Federated (apparel stores) in Manhattan have been off by 40 percent since the World Trade Center attacks. Some industries have been hurt more than others. For

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example, airlines have obviously been hurt the worst. Their share prices have been cut in half, and they have laid off around 100,000 workers. They hope that the government will provide $24 billion in aid, and airports have asked for a additional $1 billion in aid. It has been suggested that the United States will require a stimulus of $50 billion to improve its sagging economy. Including tax cuts, the figure may be twice that. Insurance companies will lose about $30 billion to cover damage claims, and many bank stocks will suffer. Travel agencies are losing $400 million a day. Restaurants are also hurting because people are dining out less since the attacks. The governmental surplus, once expected to be $300 billion at the start of the fiscal year in October 2002, may well be zero.

Near term, things may get worse before they get better. Florida's main industry is tourism, bringing about $50 billion in visitor spending to the sunshine state. Some 55 percent of Florida's 72 million tourists annually travel here by air. At least 15 percent of Florida's visitors come from New York, and they, among others, are understandably nervous about flying. Hotel bookings are well below normal, although it is too early to know if the usual winter tourists will or will not arrive. Theme parks were already doing poorly, although a recent report from Disney did show a more optimistic performance. Currently, tourism spending is down by a third, or some $20 million a day. This means local jobs get reduced or cut, and as one group gets cut, so another will feel it as the multiplier effect plays out. Tourism supplies at least 15 percent of Florida's sales tax revenue, so fewer tourists are felt immediately. Before the attacks, Florida had a budget shortfall of $265 million, but this could at least double and some say triple.

Construction and housing markets will also suffer as people wait to see what will happen in the war. The NAHB Housing Market Index is at 55, its lowest since January. Reduced consumer spending will be reflected in fewer housing starts, vehicle purchases, and household effects. Some companies are now acting to stimulate sales with special promotions. For example, GM is offering zero interest rates on all its U.S. models. Florida's retirees, who account for nearly 20 percent of the state's population, the highest in the nation, have considerable influence on Florida's economy. Sensing an attack on Social Security and facing reduced yields on their bonds and share prices on their equity holdings, they will wait, if they can, for better times to spend. Florida also has a great deal of unskilled labor, and these jobs are always the first to get hurt as unemployment continues to increase. While Florida can weather recessions better than most, the past bull market has encouraged living standards that will be difficult to maintain, particularly as the state is likely to reduce benefits.

What will get us through this crisis will be budgeting, perhaps some belt tightening, and a realistic reduction in future expectations. The financial underpinnings of the economy are strong and this storm too will be weathered.

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