

oil consumer in the world. Based on a report by IEA, oil demand growth in the United States was reduced to 100 kb/d this year, while the figure was 470 kb/d four years ago.

3. The global oil demand was averaged at 1.15 mb/d for the past 4 years, while it was 0.5 mb/d this year.

4. The global oil demand growth is projected to be some 500 kb/d next year. Some analysts predict this figure to be zero.

Now, let's deal with oil prices:

1. Obviously increasing supply coupled with decreasing demand will draw down the prices. OPEC oil basket price has already dipped to below \$20 a barrel.

2. OPEC seems to forget defending 22 to 28 dollars price band gradually. From the beginning it was clear that such policy lacks a strong theoretical back up.

3. In its meeting on the 26th September, OPEC did not make any decision to bolster the prices, but on the contrary, by putting emphasis on meeting sufficiently the developed countries needs, it weakened the prices.

In the second scenario, the assumption is based on a probable disruption of the Persian Gulf region oil exports.

1. The aforementioned analyses suggest world's readiness to put up with a 2mb/d cut from the Persian Gulf region. In this case, oil prices will be set at \$20 bbl after several days of spiking and will remain at this level for some months. The price of \$20 bbl is fully compatible with the non-OPEC producers' policies of investments in exploration and production.

2. It should be observed that, the industrial countries are currently facing

two major problems:

Firstly, the continuation of the current situation causes oil prices to fall to \$15 a barrel or even lower than that. Which is quite desirable for the global economic recession.

Secondly, the oil prices of \$15 per bbl or below may bring about a recession in oil industries in the countries such as America, Canada, Russia, and other regions where production costs are high. Such recession will aggravate the economic recession.

In summary, it seems that the industrial countries will need cheap oil for several months to come. But it should be kept in mind that in the first scenario, that is cheap oil, it does not mean anything but a monetary pressure on Iran's economy. But in the second scenario, though the reduction of exports from the Persian Gulf guarantees high oil prices, it brings about too many risks. ■

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production capacity are not willing to invest using bank credits. Therefore, reducing interest rates does not necessarily bring about an increase in investments or demand. Lack of consumer's confidence in economic recovery, as well as the probability of terrorist attacks make policy of reducing interest rates less effective.

In assessing the policy of cutting taxes, the following points are notable:

1. Before the 11th September, they were planning to cut taxes by 0.6% of GDP in order to abate the economic crisis. However, after the 11 September, taxes were cut by 1% of GDP, that means a sum of \$130 billion. Under such conditions, the U.S. budget will face a deficit rather than a surplus.

2. Implementation of monetary policies are easier than the financial ones, because contrary to financial policies such as changing government expenditures and taxes, monetary policies have better flexibility and are restorable. That is why Alan Greenspan, the head of Federal Reserves, has warned against financial policies. On the other hand, a considerable increase in government loans may result in increasing interest rates of bonds and neutralize advantages of the policy of reducing interest rates to a degree.

3. There is a risk that the policy of cutting taxes in order to either help low-income families or increase investments will be unsuccessful in increasing demand. While enterprises are facing excess production capacities, they show little tendency towards investments and the policy of cutting taxes does not guarantee any increase in this regard. Distrust in the future, leads families to save rather than spend money retrieved by cutting taxed. That is why Alan Blinder, an economist in Princeton, suggested that government should cut sales taxes rather than direct taxes so that people are discouraged to delay their purchases. This approach may increase the total demand more effectively and will not damage the government budget structure in the short run.

4. Following the 11th September, European policies to stabilize financial situation may become more flexible. According to the financial regulations, an EU member can have a budget deficit of above 3% of GDP only under emergency circumstances. Before the 11th September attacks, Germany was determined to reduce its budget deficit to 1 percent of GDP in 2002, but now it may be forced to accept 2.5% of GDP.

D. Effects on the Economy of Iran and Oil

Apart from conventional effects of war in Afghanistan on its common border with neighbours, if the U.S. military conflict is contained within Afghan borders, Iran's economy will not be affected by such movements. But, if such military operations spread to the Persian Gulf oil, then Iran's economy will be severely affected.

There are two probable scenarios concerning oil situation:

1. The continuation of the current situation, and

2. Affect on the crude oil exports in the Persian Gulf.

In the first scenario, the assumption is that, under the current situation, oil prices will fall to \$15 and lower. Fundamentals play the main role here.

Let's start with the supply side, where the oil market is facing a surplus. The following facts are notable in this regard:

1. Quota violations by the OPEC member states of about 500 kb/d (1 mb/d by unofficial statistics), form a surplus market.

2. Non-OPEC production (the USA, Canada, the North Sea, Africa, Russia, ...) have increased by 500 kb/d since last year due to surging oil prices. Some projections see non-OPEC production in 2002 as 800 kb/d. Russia is steadily increasing its production.

3. Stocks are high. The policy of OPEC has always been to uplift stock consumption by cutting production. Expecting this to result in checking the fall in prices. However constant quota violations by members failed the policy.

4. Investments' by some OPEC member states to increase their surplus production capacities are significant. Such investments imply the existence of more supply in the horizon, therefore, oil prices will tend to fall. Other facts such as Saudi Arabia's excess production capability of 2mb/d and Iraq's readiness to increase its production are among other factors to convince market of the prospective supply surplus and thus lower prices.

In this section, we turn to the demand side where the global oil market is facing a slump. Noting the following factors can be helpful:

1. A decrease in the growth of global economy causes a fall in oil demand accordingly.

2. The United States is the biggest

**the U.S. government policy
relies on three elements:
reducing interest rates,
cutting taxes,
and increasing expenses**

thousand feet even in the dark and under bad climatic conditions.

e. Effects on Global Economy

Before the 11th September attacks, global economy looked bearish. Now whether recent events may exacerbate the crisis at international level or conversely they can bring about briskness to it, remains to be answered. However, in answering the above mentioned question, three important points should be noted:

Firstly, all developments in the U.S. economy do have a great impact on the world economy and in particular on that of the industrial countries. In fact, if parties to the U.S. foreign trade predict that a recession in the U.S. economy is inevitable, then they surely reduce their investments and exports to America, thus worsening the situation for their economies.

Secondly, American consumers' expectations play a key role in the boom and bust of the U.S. economy.

Thirdly, the war efforts in Afghanistan and the likelihood of its spreading to other countries in the Persian Gulf are considered as pivotal parameters in analysing the economic aftermaths of the 11th September attacks.

At first, we try to elaborate on the role of the U.S. consumer's expectations:

1. Before the 11th September, the U.S. consumers' confidence in the business and high rate of consumption prevented a serious economic crisis in the U.S., despite the increasing rate of unemployment and steady reduction in industrial production. How will recent events affect the U.S. consumers' expectations and their confidence in the future economic developments remain to be seen.

2. Industrial countries are currently so sensitive to terrorism that consider any bane rooted in it. For example, the crash of a flight from Israel to Siberia on the 14th October which killed 76 people, was first interpreted as a terrorist attack, while it was due to a strayed missile during a military exercise in Ukraine. This accident coincided with Blair's imminent trip to visit Putin while, at the same time, the U.S. Secretary of Defense, Ramsfeld, was planning to visit Saudi Arabia, Oman, Egypt and Uzbekistan.

We can conclude that, worries due to terrorism push American consumers to distrust the future, and the ensuing reduction in their spendings will exacerbate the U.S. economic crisis.

In this section, let's deal with the U.S. military operations in Afghanistan:

1. Based on the existing evidence, it can be deduced that the U.S. military intervention in Afghanistan is merely to prepare the ground for a long-term presence of the U.S. forces in Afghanistan so that the U.S. government can achieve its security and political goals in the region. It is obvious that a long-term presence in Afghanistan requires either establishing friendly relations with the Taliban regime or replacing it.

2. With this assumption, the U.S. military presence in Afghanistan may have nothing to do with the global economy. However, increasing defense

expenses due to the U.S. military presence will raise demand and may alleviate the current economic crisis.

3. The assumption of war spreading to the Persian Gulf region will be discussed later.

C. The U.S. Economic Policies for Coping with the Economic Crisis

The U.S. economic policies hinge on increasing demand and recovering investors and consumers' confidence. To achieve their goal, the U.S. government policy relies on three elements: reducing interest rates, cutting taxes, and increasing expenses, especially defence expenses.

First let us discuss the U.S. policy of reducing interest rates:

1. Before the 11th September, the U.S. financial and monetary officials had already reduced interest rates six times to abate the crisis. In their seventh and eighth attempts immediately after the 11th and on the 17th September, several hours before the stock market business resumption, they reduced interest rates by more 0.5%. Some hours later, European Central Bank which had opposed any reduction in the interest rates reduced their interest rates by the same percentage. On the 18th September, Switzerland, Canada, and England reduced their interest rates too.

2. After nine times of consecutive reduction in interest rates, they are currently at 2.5% suggesting a remarkable reduction in comparison with the end of last year interest rate of 6.5%. As a matter of fact, interest rates have reached their lowest level in the past 40 years.

3. In view of the existing commodity price index, it seems that the real interest rate in America is close to zero.

4. It is likely that reducing interest rates may not sufficiently increase demand. Enterprises facing excess

On 19th September, United Airlines and American Airlines cut more 20,000 jobs each

Meanwhile the number of flights within Europe and the United States were reduced by 12% and 4% respectively. The total loss incurred by airlines during 1990 -1993 period reached \$15 billion.

6. The U.S. Congress passed a bill in September obliging the U.S. government to pay the extra insurance fees for airline companies for 180 days and bear all losses due to terrorist attacks and war, provided the damages exceed \$100 million.

7. Airline companies have only been able to cope with the crisis by cutting more jobs. On 19th September, United Airlines and American Airlines cut more 20,000 jobs each. BA laid off 5200 of its workers (in addition to 1800 jobs previously cut).

8. Considering the rising charges due to enforcing safety regulations and precautions against terrorist attacks, on the one hand, and the increasing risk of flights to America, on the other, it seems that adopting the policy of merging airlines is inevitable. The idea of such mergers goes back to some time before the 11 September attacks. The main reason behind this idea was the imminent recession for the U.S. airlines. United Airlines was determined to acquire U.S Airways, but their plan was foiled by some legal obstacles. However under current conditions, legal obstacles seem to be less effective in such mergers.

9. It is likely that American Airlines and BA merge their cross-Atlantic

flights and so will Delta Airlines and AirFrance.

10. The activity of factories specialized in making airplanes will be restricted. Boeing Company is planning to cut 30,000 jobs in 12 months, because the number of orders fell drastically. The company is going to reduce its production from 500 planes in this year to 400 in 2002. In 2003, Boeing is scheduled to produce only 350 Planes. Obviously, increasing the production of war planes could be a way out.

d. Effects on Military Industries

Although the impacts of recent events on military industries is not very clear, a remarkable change in production patterns in the U.S. and European military industries is likely.

1. Producing advanced topography instruments, satellites or unmanned aircrafts for reconnaissance missions or even unmanned fighters will be of higher priority than ordinary war ships and fighters.

2. Forming a counter-terrorism coalition may get countries on both sides of the Atlantic to cooperate closer together in order to promote joint planning for military technology, although, the U.S. government still wants to retain its supremacy.

3. The U.S. four-year defence plan has recently been revised putting heavy emphasis on confronting unusual threats and hostilities such as terrorist attacks. Most European countries have increased their defense budget.

4. Stock markets reacted to such changes in policies rising shares of such enterprises as Raytheon and Northrop.

5. Following the end of the Cold War, defence budgets on both sides of Atlantic were reducing steadily. The U.S. defence budget reduced to as low as 2.4% of GDP, while under the Ronald Regan administration it was about 6.4% of GDP. In other words,

the Pentagon spent annually \$120 billion then, the figure is \$42 billion a year now. Considering recent events, a revised \$60 billion defense budget seems to be predictable.

6. Perhaps the U.S. bombers should be replaced earlier than their due lifetime. Also, Boeing has received an order from the Pentagon to speed up producing 60 gigantic C-17 military airplanes specialized in carrying tanks.

7. Military hard wear producing companies in Europe, especially is England (BAE) and France (Thales) are watching the U.S. military and political developments with the greatest concern. Both John Weston, CEO of BAE, and Denis Ranque CEO of Thales, believe that the U.S. market will be their biggest market for the next 50 years. At present, BAE sales to the Pentagon exceeds their sales to British Ministry of Defence. Thales which has sold their latest technological achievements in electronic warfare to the U.S. government, believes that the 11th September was a turning point in defence industries since from now on technology will have the final say in the military industries.

8. Recent events may bring about a much closer cooperation between the U.S. and European defence industries. Producing new aircrafts by Boeing in collaboration with BAE; cooperations between Raytheon and Thales in introducing new generation of RADARs; and joint attempt of Northrop and EADS to make Unmanned Aerial Vehicles (UAVs) are notable in this regard.

9. Some of recent technological achievements will be tested in Afghanistan. For example, a type of Unmanned Aerial Vehicles, Global Hawk, has been sent to Afghanistan. This aircraft is capable of flying up to 36 hours non-stop and can easily reconnoiter from the altitude of 65

insurance commitments for airlines against terrorist attacks up to \$1 billion.

13. Since the 11th September, a very important question has been raised whether insurance companies will be able to pay compensations due to nuclear, chemical or biological attacks? Maurice Greenberg, the director of AIG believes not. He holds that governments themselves should play the role of final insurer against such risks.

14. Establishing insurance companies specialized in terrorist attacks seems to be inevitable in the U.S. Similarly, in the U.K, IRA military operations resulted in the creation of Pool Re insurance company. France and Israel are among the countries with valuable information

and experience concerning such insurance companies.

c. Effects on Airline Companies

Before the 11th September, airline companies were already on the verge of recession. They were projected to suffer a loss of about \$3 billion in 2001. Nevertheless, the 11th September attacks have doubled their burdens.

1. The U.S. airline companies lost \$650 million only within a few days after the attacks.

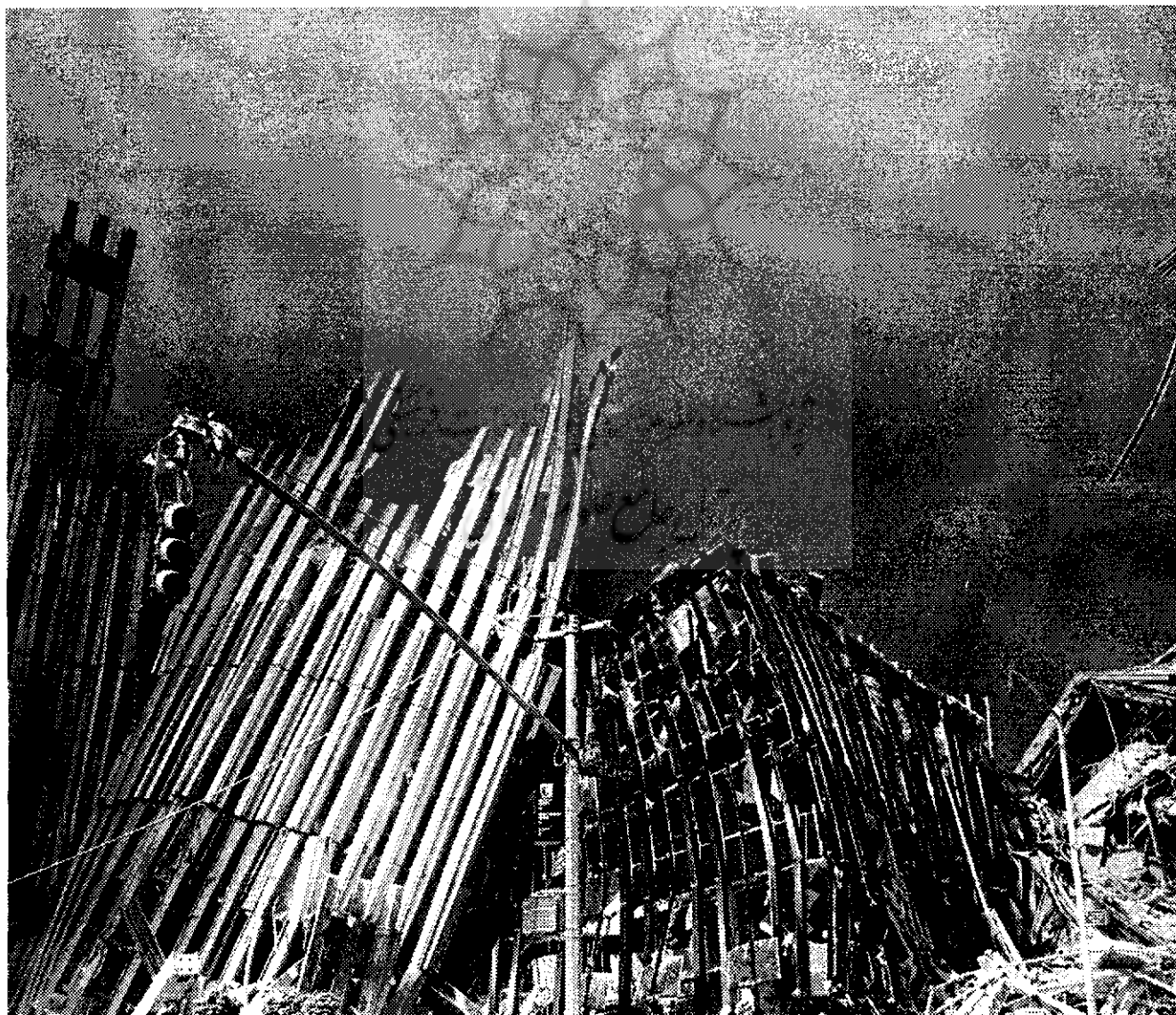
2. Even now, more than a month after the attacks, most flights are half loaded and reservation fees have tumble severely. The profitability criterion of a flight is defined as loading at least three

forth of the flight full capacity. Even a 5% reduction in demand can cause a loss for an airline.

3. Based on a report by the International Airline Trade Association, airlines incurred some \$10 billion loss due to the 11th September attacks. This amount of loss will effect the United States, Europe and Asia.

4. Among European airlines, the ones that have more of cross-Atlantic flights are in greater losses.

5. Airline companies have experienced near such losses earlier, for example, during the Persian Gulf war in 1991, the number of cross-Atlantic flights fell by some 25%. Flights from Europe to the Middle East fell by 55%.



Comparing with the crash of stock prices in 1987 recent sagging share prices may be considered less significant

spaces in these towers. Main insurance brokers of major insurance companies, such as McLennan, Anon & March were in the WTC. Surprisingly, the New York World Trade Center was the target of three bombing attempts in the 20th century.

5. Total disruption of communication between the WTC and 320 trade centers around the world and complete break down of the WTC information network was another blow across the stock and financial markets.

6. The immediate effects of this destruction on companies using very short-term credits were considerable. The New York Bank was damaged heavily in comparison with other banks, for its principal bureaux were in the twin towers' neighborhood. In total, it is said that e-commerce transactions fell by 70% after the attacks.

b. Effects on Insurance Companies

1. The 11th September attacks served the largest blow to the insurance companies. The damage is estimated to be in range of \$30 to \$40 to even \$70 billion. The leading insurance company, Lloyds of London, suffered the greatest loss.

2. Considering the high death tolls, insurance companies have to pay considerable sums of money for lost

lives. Especially, compensations to be paid for many managers range from 1 to 5 million dollars each.

3. Damages for physical and mental losses and payments to those survivals who will probably be out of job for a long time, sums up a considerable amount of money.

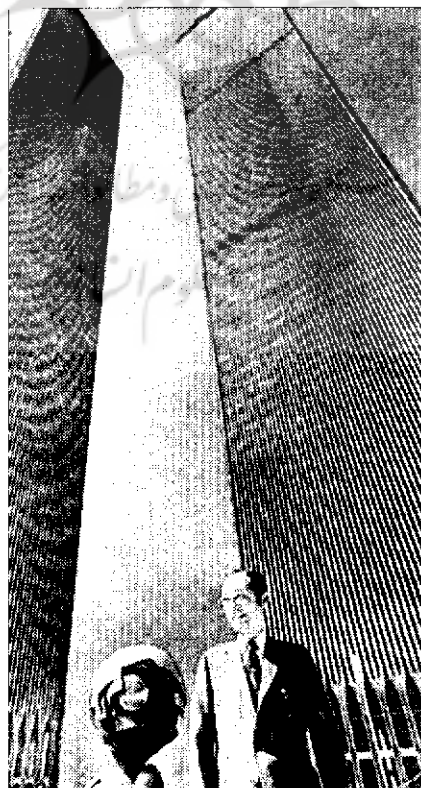
4. The twin towers were insured for \$3.2 billion.

5. Airline companies whose planes were hijacked, were insured for \$1.7 billion.

6. Any interruption to the normal process of trade requires a considerable compensation.

7. Insurance Information Institute has reported that many legal cases regarding such insurance policies will be settled in the next two or three months; however, there are some cases that might take several years because insurance companies may claim that their insurance policies did not cover war conditions.

Earlier, in Lockerbie case, insurance



Mr. Yamasaki;

The architect of the Twin Towers

companies put forth different legal arguments regarding the coverage of losses due to terrorist attacks by their insurance policies, and they succeeded to delay the payment of compensations for some time. Since, in his speech, the U.S. president regarded the attacks on the WTC twin towers as Acts of War, insurance companies find themselves in a strong position. It is worth mentioning that American insurance companies generally include terrorist attacks in their insurance policies, but their interpretation of terrorist attacks and whether they include attacks on WTC twin towers or not is open to question.

8. Some of the leading insurance companies, such as Guy Carpenter, Anon and Royal & Sun Alliance were located in the twin towers and obviously lost a lot.

9. It is customary that insurance companies are reinsured by other insurers so that they guarantee their payments in case of huge damages. Therefore, damages due to the 11th September attacks will be shared by insurance companies and their reinsurers.

10. After the 11th September, insurance companies, on the one hand, raised immediately their insurance fees for airline companies and, on the other, lowered their payment of compensations to as low as \$50 million for each terrorist attack.

11. It seems that the business of reinsuring other insurance companies will grow rapidly in the future and reinsurance will accelerate structural changes in insurance companies. Besides, studies related to insurances against terrorist attacks will have a special place in the insurance industry.

12. On 25th September, American International Group (AIG), the biggest insurance company in the United States, announced that by raising insurance fees they will be able to extend their

This report has been prepared by Dr. Masoud Drakhshan and translated from Persian into English by this monthly, reviewing economic aftereffects of the 11th September attacks, comprises four chapters. First chapter deals with global economic situation before the 11 September attack and yields an analysis framework to survey the economic aspects of those attacks. It tries to assess the extend to which employed

policies have been effective. The short term impacts of recent tragic events on stock and financial markets, insurance companies, airlines, military industries and global economy, are discussed in chapter two. Chapter three surveys the U.S. policies in coping with the recent economy crisis. Chapter four looks at the possible upshots of recent events on Iran's economy or on its oil industry.

A. Global Economy before the 11th September Attacks

In late 2000, the possibility of the U.S. led developed economies of the industrial world dip into a recession was looming. In this regard following facts would be notable:

1. Statistics published in September 2001 reveal that America's industrial production rate has been shrinking for the 11th consecutive months which is regarded as the longest period of production reduction since 1960. Industrial goods production annual rate reduced by 4.8% by the end of August.

2. In August 2001, rate of unemployment was at 4.9 percent, the highest rate in last four years.

3. America's economic growth rate from September 2000 to September 2001 was projected to be above 3 percent; however, it was reported to be 1.7 percent in September 2001. Within the same period of time, the actual economic growths of Euro area and Japan were %1.8 and %0.5 respectively, despite the fact that they were originally announced to reach %3 and %2.

4. Industrial production stock shown in major indices such as Dow Jones, Nasdaq, and S&P 500 were shrinking steadily throughout the year ending in September 2001.

5. The only remarkable exception was the value of the shares of oil

companies which reported surge in profits despite the global recession. This could be accounted for by OPEC's decent policies. Shell, for instance, reported for the first six months of the year a profit 15 percent higher than last year. While Shell's profitability last year had reached its the highest since 1998 oil price crisis.

B. Short-term Effects of 11th September Attacks

Apparently, economic authorities have been trying to calm down the global economy. For example, managing director of IMF announced on 12th September that recent events have little effect on global economy, and there is no reason for concern. Likewise, Secretary General of OPEC, declared that under such conditions, OPEC sees itself more committed than ever to securing global oil demand in full.

a. Stocks and Financial Markets

1. Soon after the 11th September attacks, major stock markets closed. This reaction is considered to be very significant. Because, last time when New York Mercantile Exchange (NYMEX) closed for several days, it was due to the assassination of president J.F. Kennedy (in 1963).

2. When the stock exchange markets reopened on 17th September, stock

indices tumbled (Dow Jones and Nasdaq 7%, S&P 500 about 5%). Such descending trend went on until 21st September when stock indices made a V-shape bounce back. Currently, they are at the same level as they were before the 11th September. However, it should be noted that some airline companies' shares tumbled by 40%, while weapon producing companies enjoyed an increase in their shares.

3. Comparing with the crash of stock prices in 1987 when Dow Jones, for instance, fell by 22%, recent sagging share prices may be considered less significant. Nevertheless, on 17th September 2001, Dow Jones index fell by 20%, down from the previous maximum value. Such considerable shrinkage reveals that the 11th September was a coup de grace for stock markets already on the verge of recession.

4. The demolition of the World Trade Center twin towers brought about some disruptions to major stock markets. For example, Cantor Fitzgerald, the biggest broker of the U.S. exchequer bills was located in the top floor of one of the towers. Future Markets of the U.S. exchequer bills was located in the lower floors of these towers as well. Besides, a huge financial organization, Morgan Stanley, which was considered to be among the key players of stock markets, occupied most of the rental

Review of Economic Aftermaths of the 11Th September Attacks

PLANES SLAM TOWERS ...

8:45 a.m.
American Airlines Flight 11, a Boeing 767 hijacked en route from Boston to Los Angeles with 92 passengers aboard, slams into the north tower

9:06
United Airlines Flight 175, also a Boeing 767 hijacked en route from Boston to Los Angeles with 65 passengers aboard, banks hard and slices through the south tower

... AND WEAKENED BUILDINGS COLLAPSE

10:00
The sudden collapse of the south tower traps hundreds of workers below. In addition to perhaps thousands of workers in the building, debris guts the 4 World Trade Center building below

10:29
Weakened by its imploded twin, the north tower collapses, raining more debris and crushing buildings and workers below

5:25 p.m.
As fires and debris finally take their toll, the 7 World Trade Center building falls

FIRST IMPACT

American Flight 11

WHO WAS INSIDE
The Port Authority of New York and New Jersey leased six floors of the north tower. Cantor Fitzgerald Securities, on floors 101-105, cannot account for 1,000 of its employees

1 World Trade Center

Second to collapse
Completed: 1970
Height: 110 floors
Floor Sizes: (8,108) 45,000-50,000 sq. ft.
Elevators: 97 passenger, 6 freight

2 World Trade Center

First to collapse
Completed: 1972
Height: 110 floors
Floor Sizes: (2,108) 45,000-50,000 sq. ft.
Elevators: 97 passenger, 6 freight

7 World Trade Center

Third to collapse

WHO WAS INSIDE
Morgan Stanley Dean Witter was the single largest tenant in the south tower, leasing 21 floors. Both buildings hold 50,000 people

SECOND IMPACT

United Flight 175

PLAZA

All tower buildings around the plaza virtually destroyed by falling debris

Marriott Hotel

WHY DID THEY COLLAPSE?

Each of the towers, more than 200 ft. wide on each side, contained a central steel core surrounded by open office space. Eighteen-inch steel tubes ran vertically along the outside, providing much of the support for the building

Once the plane damaged the central core, the weight was redistributed to the outer steel tubes, which were slowly deformed by the added weight and the heat of the fires

Source: Port Authority of New York and New Jersey; Associated Press; Supplement by Julie Dwyer, Associated Press; by Joe Myers and Scotter

IME Graphics by Ed Savel