

WORLD AND ALBANIAN ECONOMY AFTER THE TERRORIST ATTACKS OF SEPTEMBER 11, 2001

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Keywords

- Terrorist attacks - Stock markets - Exchange rates - Economic slowdown -

The terrorist attacks of September 11 in New York and Washington are considered as a shock event for the United States and for the whole world economy.

Nevertheless, the ensuing period (September 11 and ahead) had some distinctive moments that can be divided as follows:

1. The terrorist attack on USA (September 11).
2. The false news on the starting attack of United States against Afghanistan (round September 21 and October 1).
3. The starting attack of United States against Afghanistan (October 7).

As stock markets represent the most sensitive and perhaps the most accurate thermometer of the political and economic situation worldwide, the following summary starts the introduction of the shock impact, precisely, with a description of stock markets around the world.

A. STOCK MARKETS

1. STOCK MARKETS OPENED IMMEDIATELY AFTER THE ATTACK - SEPTEMBER 17, 2001

The decision for not opening markets until September 17 could not prevent the expected decline in share prices. In the first day of activity, Wall Street recorded a declining index of Dow Jones with 7.13 percent and NYSE index by 6 percent. The first companies to lose points in the stock markets were air companies and the big insurance companies. Directly injured from the terrorist attack were many financial companies suffering considerable material and human losses. A similar attack on the United States was unique. Moreover, from the type of the attack, the American people and policymakers highlighted the feeling of patriotism and solidarity. Although anyone could scarcely think of an incentive for purchasing shares as inspired from patriotic feelings, it was precisely that that happened in the first days of the opening of stock markets all over the United States. Perhaps the reduction of stock prices would have been higher at the deficiency of immediate coordination of expansive policy of Federal Reserve and the confidence injected in the capital markets through appeals and actions that supported the stocks purchase.

At the same time, looking with optimism the Federal Reserve's 17 September decision to reduce the money cost by 0.5 percentage points made the stock markets in Europe have a positive reaction recouping within the second half of Monday all losses suffered at the beginning of it. Concretely, Milan stock market recorded 0.17 percent increase, that of Paris +2.3 percent, London Stock Exchange +2 percent and that of Frankfurt + 2.9 percent.

2. THE END OF THE FIRST WEEK AFTER RE-OPENING

September 21 did not mail good news for stock markets all over the world. In the meantime, in New York excavations

continued under the World Trade Center. Various messages related to the United States' attitude to Afghanistan arrived from politicians and media. The fear that a merciless attitude of USA would instigate the same ferocious and unpredictable stand on behalf of terrorists made the stock markets list the lowest points at the end of the week. Shareholders, scared from what might be happening in the next two days (when stock markets were closed), hurried to largely sell their shares enforcing the stock markets record losses that varied from 5-7 percent at the end of the day. As the expectancy of declaring war from United States would not suffice that, the European stock markets found themselves in front of many technical problems and false alarms for bombs or surprise attacks. The idea in that time was that the European and United States stock markets had entered into a vicious circle that made the losses of one party be constantly reflected to the other and vice-versa.

After the lowest point reached in September 21, USA, London, Paris, Japan, Germany, Italy stock markets, etc., started a slow and insecure recovery, hoping that the suffered losses during the previous week would be recouped soon. Anyway, forecasts on the date of expected attack from USA over Afghanistan became a ruthless factor for the stock markets. So, on October 1 in response to expected attacks, NASDAQ lost 2 percent whereas Milan Stock Market, 2.2 percent. Almost the same movements were noticed in the rest of the stock markets all over the world.

The most sold out shares in the precise moment corresponded to high technology and telephone companies. The expected attack of USA was not the only cause for the reduction of share prices; the further coping with deep financial troubles from European and American companies was another cause of it. Some of the companies to be really put in financial difficulties were the British Airways, "KLM", "Swissair" and "Lufthansa". These companies requested financial support from the European Commission for Transports in Brussels. The latter did not consider their requirement pretending that no federal budget existed for European companies to support them in case of financial difficulties. The same scenario was noticed in USA

one week before. The difference in this case lied in the fact that the Congress credited the air companies put in financial difficulty with USD 15 million, from which 10 millions were soft-term credits.

With the passing of shock moments, stock markets came back to normality; surely, the experience of September 11 taught them something to learn forever.

B. EXCHANGE RATE PERFORMANCE

If taken a fast glance to the exchange rate performance by the international markets worldwide, we will come to the conclusion that the US dollar began to lose grounds against the Euro and the Japanese Yen (JPN), British pound (GBP) and the Swiss currency (CHF) from the end of June. The Euro, CHF, USD revealed signs of recovery by the end of August. This phenomenon can be explained with the more optimistic messages, arriving from the United States economy in this period. The idea that the economy potential would enable a fast and stable emergence from the difficult situation continued to be spread and believed to the moment when the unexpected attack hit the United States.

In the days that the United States stock markets remained closed, foreign exchange markets all over the world priced the new values for USD exchange rates to the rest of the currencies. It was precisely in these days that, the deceptive news on the starting attack of United States against Afghanistan was squeezed into the written and electronic media.

Table 1. Some currencies' exchange rates to USD during the lowest point days

The days with the lowest point of USD	Currency	Value to USD
September 19	Euro	1.08015
September 20	JPY	115.85
September 21	CHF	1.587
October 5	GBP	0.6759

While the Euro currency was faster, the British pound took two days to spin the USD at its lowest point in the last months.

From 19 September, the USD gradually strengthened to Euro, although its exchange rate displayed slight oscillations.

The current performance suggested a further strengthening of the USD or at least maintaining of its current value, although the last thing to be mentioned in the forecast corresponds to the way these economies, based on each of these currencies, will be developed. Almost the same scenario has taken place between USD and JPY currencies, with the only change that the USD appreciation was faster than the Euro, after September 20.

While the USD appreciated by 3.4 percent to EURO between September 19 and 25, it gained 6 percent of its value compared to JPY for the same period.

JPY also reached its top in exchange with EURO between September 19 and 20, but next months' developments cited a strengthening of the Euro currency to the Asian one. The CHF won over the USD or the Euro in the same day and its exchange rate to either USD or Euro was by 0.630 or 0.692 respectively. It must be said that while the USD was slower in reaching this point, EURO suffered an immediate discount within 3-4 days. CHF is gradually depreciated to the USD; however it remains still stronger from what it has been before September 11.

Related to CHF/Euro exchange rate, it has been noticeably more favourable to CHF from what it has been before September 2, confirming a further depreciation of the Euro.

The GBP started appreciation against the USD from the end of May, when 1 USD was exchanged with 0.723 GBP. Until today, this remains the USD's highest point during the last six months. On October 5, it reached the lowest point of 0.675 GBP, to further climb up to the level of the beginning of August.

After its lowest point to GBP on October 5, the Euro continued its decline against the GBP. The news on the British economy is more optimistic from those arriving from the rest of the Western Europe and Germany, especially. As evidenced from

the above developments, all powerful currencies worldwide reacted against the green currency, leading it to the lowest points surprisingly not at the initial moment when the false news on the expected war and the guesses on the terrorists' reaction caused fear and insecurity all over the world. From this complex picture of international markets, it might be assumed that the psychological effect and expectations play a very important role in the exchange rate performance.

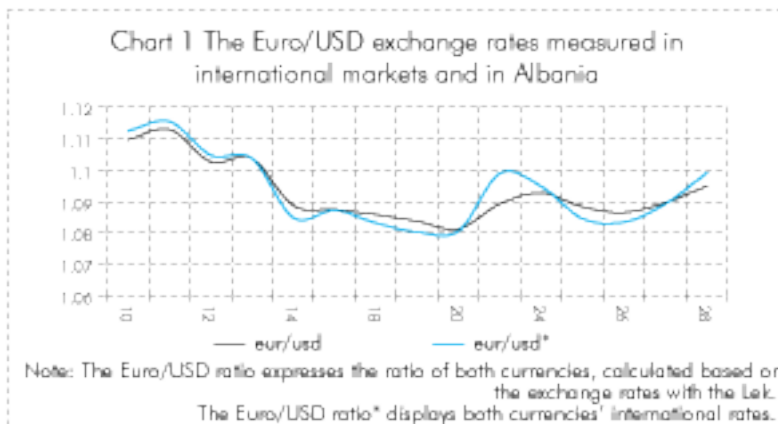
C. THE FOREIGN EXCHANGE MARKET IN ALBANIA

Before passing to the consequences that the terrorist attack had on the United States currency exchanged in Albania, it must be said that the USD did not recognize positive developments in two months prior to the terrorist attack. The Lek/USD average rate in June was 148.55. It was a long time before, since October-November, previous year that USD did not record such a high rate.

June recorded the USD's last strongest point, which started to fall against the Lek, passing to the average of 147.8 Lek in June and 143.35 in August. It is understandable that besides the seasonal factors, such a situation was amply conditioned by the constant weakening of the United States economy, faithfully reflected in the USD/Euro rate. As it happened in the international markets worldwide, the USD also lost ground in the Albanian market during these months. The USD exchange rate was 126.8 Lek in June, 127.2 Lek in July and 128.9 Lek in August.

The terrorist attack on USA was first of all reflected in the instant decreasing value of the USD. In the subsequent fortnight, newspapers, released for public opinion, published headlines that still more added the public mistrust to the green currency. Still, according to these papers publicity, USD enjoyed "the heavens" in the Albanian market, only a few months ago. The psychological effects played a negative role in the USD's performance against

the Lek. In the second week after September 11, the USD lost 1.67 percent against the Lek, passing from 144 Lek/USD to 141.63 Lek /USD (September 21). The following chart presents the Euro/USD behaviour in the period of September 10-28, 2001.



As evidenced from the above chart, the Lek/USD and Lek/Euro exchange rates during September have generally followed the same developments with those of the international markets. After this date and after the low exchange rate it had in the previous day, the USD appreciated immediately, being exchanged at 1.099 Euro in the world markets, while the same ratio recorded 1.089 in the Albanian market. The USD reached its lowest rates to Lek. On September 17, 20 and 26, it was exchanged at respectively 141.35, 141.37 and 141.21 Leks. September 20 has also recorded the highest monthly value for the Euro (130.75 Lek), the monthly average for both currencies was at 142.89 for Lek/USD and 129.83 for Lek/Euro.

During the current month the USD oscillated between Lek 142.26 and 140.66 rates. The last figure corresponds to October 9 and it was the lowest value attained throughout the month. In the meantime, the European currency moved through the values Lek 126.11 (October 26) and Lek 129.7 (October 5).

From these developments it seems that the Albanian foreign exchange market has moved in accordance with the international exchange market and has reacted to the developments noticed in this market.

D. THE CENTRAL BANKS' REACTION AGAINST THE TERRORIST ATTACKS OF SEPTEMBER 11 AND AHEAD

“The Federal Reserve System is open and able to work, whereas the discount window is ready to cover the needs for liquidity”. This was the only statement released by the vice-president of the most powerful central bank in the world in the afternoon of September 11, 2001¹. And it was also the same statement that made possible the injection of USD 80 billion in the United States' financial system to the end of this uncommon day. At the same time, the managerial authorities of the European Central Bank confirmed the ECB's readiness to provide the required liquidity from the European financial market. The German Bundesbank from this day acted as the greatest supplier of liquidity and in a few days it cleared through its clearing system an amount of USD 500 billion.

One day after the terrorist attacks, finance ministers and central bank governors of G-7 prepared a rescuing plan, including diminished costs of borrowing, aiming at adding liquidity in the market and encouraging the economy. The stock market closure during the first week let free way to several suspects and speculations regarding further developments in the stock market indexes. The prevailing fear and panic would lead to distinct prices of equity securities from the massive sales.

In this point the pressure exercised on the Federal Reserve to have an immediate cut of interest rates was very high. Perhaps, the only reason why the envisaged and almost certain reduction was not effected was some American experts' impression that such a step, taken at the moment when the United States were still

under the shock of views from the attack and the stock markets were not opened yet, would not have the expected impact on the financial markets. Apart "When?" the Federal Reserve also made another inevitable question: "What will be happening to the rest of the world after we lower the interest rates?"

The answer to this question came no later than the beginning of the next week, immediately after the Fed declared for the eighth time during this year, interest rates and money cost reduction by 0.5 percent, bringing them down to 2.5 percent. The breaking news on the reduction of money costs was accompanied with the appeal that the Federal Reserve Governor, Mr. Alan Greenspan, addressed to banks to be more tolerant to customers put in difficult situation from the terrorist attacks. The Federal Reserve also asked all banks to be ready to credit different persons or companies presenting a pressing need for funds. With all these measures the Federal Reserve tried to encourage new investments and maintain the Americans' current consumption rate which comprises about 2/3 of GDP.

While the United States did their best to keep the economy in shape, in Europe the ECB announced the reduction of the refinancing rate by 0.5 percent half an hour after a refinancing operation was made at 4.25 percent rate. Referring to the comments of a central banker "Europe had to tell to the whole world that it was on the side of the United States". Perhaps, not so amiable questions and comments made on ECB policy were attributed to its very prudential stand held to the reduction of interest rates, while the Federal Reserve did not show the slightest indecision to follow an expansive policy throughout the whole 2001.

Besides the two greatest central banks, the monetary authorities of Japan, Switzerland, Canada and Great Britain also had an immediate reaction to the United States developments. Immediately after the attack they injected considerable amounts of liquidity. The Federal Reserve entered in swap agreement with the ECB, the Bank of England and the Bank of Canada in order to relieve the financial markets' functioning and ensure liquidity

denominated in USD. The Bank of Canada and the National Bank of Switzerland had the same interest rate cut with the Fed and the ECB. The monetary authorities of England, Japan, Denmark, Sweden, New Zealand, Hong Kong and Korea also computed interest rate reduction at a later time.

The first reaction of the central banks was welcomed from the international markets and it was considered as a powerful and required support to specific economies. To November 6, the Federal Reserve cut twice the interest rate, leading them to 2 percent rate. At the same time, the Bank of England cut short-term interest by 0.5 percentage points, leading it to 4 percent, and the ECB made the same cut with the Bank of England leading its short-term rates to 3.25 percent. While the central banks' expansive trends are being supported by those that aim at promoting the world economy, they are looked with scepticism by those that are scared from the incapacity to manoeuvre in the long run. The most negative example of it may be the case of Japan, finding itself within a prolonged period of recession.

Interest rate reductions internationally are expected to be reflected in the decreased net earnings from the Bank of Albania's foreign exchange reserves deposited abroad the country. Additionally to this effect, these cuts are reflected and continue to be reflected in deposit rates denominated in different foreign currencies and especially in those denominated in USD.

E. RECENT EVENTS IMPACT ON LOW- AND - AVERAGE- INCOME COUNTRIES

Further to the recent events the international institutions such as the World Bank or the International Monetary Fund hurried to perform revaluation of their forecasts addressed to the performance of world economy in general and that of countries in particular.

It is clear that the lag effect of the global economy on each country depends on the typical features of the country in

discussion and the latter financial and trade relationships with the rest of the world. For this reason the analysis is made separately for a group of countries attached either in geographical vicinity or other common features of economic development.

For the developing countries² where our country is included, forecasts on GDP growth for years 2001 and 2002 are reduced due to their dependency on the economic advance of the developed countries. The most direct effects of world crisis over these countries are expected to appear in some forms that will be analyzed below:

Tourism - The insecurity that besieged the world economy after the terrorist attack was translated into instant reduction of the number of travellers using airlines. The flies in the United States and those from USA to Europe and between the European countries suffered from a tremendous decline of travelling demand some weeks after the tragedy. Flying tariffs underwent a considerable decline, which depriving the air companies from profits, served to somewhat fill up the empty lines. Although the initial wavering of travellers is already mitigated, the tourists' indecision to undertake tours remains high. Perhaps, it must take a long time before the tourists' behaviour comes back to normality.

In the light of recent developments, Albania being part of the Balkans Peninsula remains in the list of the countries presenting a not so small risk, and the United States surely did not help to mollify the perception of foreign or Albanian visitors.

In the subsequent months, that is for year-end holidays, it may happen that a part of Albanian citizens already European or United States residents will not come back to meet their families in Albania, because of the insecurity to take long trips. According to the Balance of Payments definition, the services these persons buy in Albania (travelling services) are classified under the category of exported services, occupying nearly 84.5 percent of the total. Traveller exported services over the first half of 2001 reached USD 194 million or about USD 66 million

more than the imported services, making the total balance of services be positive per USD 18 million.

If the subsequent months are accompanied with a decline in the number of Albanian non-residents visiting the country, it may happen that the balance of services deteriorates or loses the function it has played until now, as a balancer of current account.

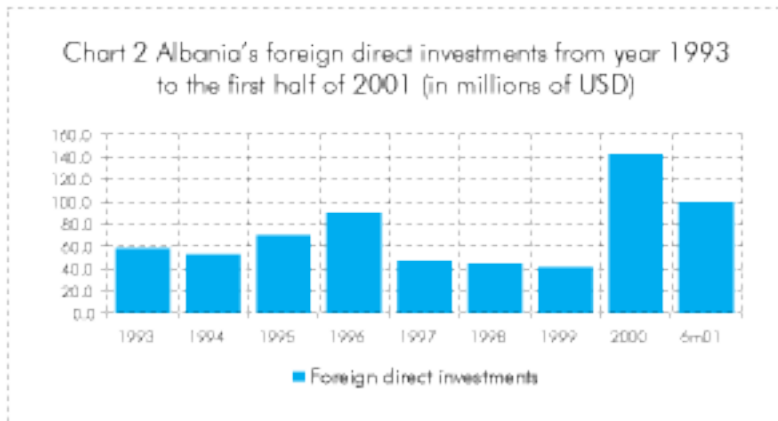
Concerning the number of foreigners visiting Albania³, it may also decline, however, the above-mentioned category, that of Albanian non-residents arriving to Albania to pass summer or winter vacations holds the main weight in our statistics.

On the other hand, if a reduction of tourism prices attracts more Albanians abroad the country, then the balance of services will probably narrow further. So the deterioration may be two-sided.

Financial markets: In September the capital market investment in developing economies indicated 35 percent decline compared to August.

While the interest rate reduction in USA in 1990 made the capital inflows have a considerable access to developing economies, the current situation may condition the level of lending and the number of countries to benefit from these funds.

Foreign direct investments, which are regarded as closely linked with business cycles in developed countries are likely to suffer decline, due to the not so positive performance of these countries' economies. Foreign direct investments do not depend only on the economic performance of the developed countries, i.e., on having or not having capital for investment, but also on the sentiment of investors which is not giving goods signs for a long time.



As clearly observed from the above chart, foreign direct investments in the country have increased in the last two years.

If the successive months are accompanied with a decline of investor's confidence worldwide and if the Balkans continues to be regarded as a hot area of conflicts, Albania's picture will probably change. What is more irksome to this forecast is the correlation between foreign direct investments and the privatization process.

While Albania is laying the grounds for the privatization of relevant economic and financial entities, the possibility for foreign investors to run away, in terms of the number or funds they offer, is not good news.

Main commodity markets - A protracted recovery of world economy might impede the increase of commodity prices, disclosing decline during the recent four years. The decrease of these prices was further emphasized after September 11, as follows⁴:

Table 2 Changes in some main merchandise goods prices

Product	Change in price (September 11 - October 24)
Oil	-4.5 usd
Rural products	-(6-8) %
Metals	-4 %

The reduction in these prices, while reflecting an advantage to the countries importing these products, it creates an unsafe situation for the export ones. Those countries that might be suffering more from the decrease of prices at the moment and further in the near future are those economies whose trade is based vitally on rural exports or textile originated products. As these countries are not big users and suppliers of oil, they do not benefit from the oil prices' decline, while they pay a fixed tax on exports' side. These developments may be regarded somewhat positive for the Albania's trade balance, due to the import/export structure presented in this way⁵:

Table 3: Weights of main group prices in Albanian imports and exports

Merchandise group	as % of total imports	as % of total exports
Oil (and power products)	8.9	1.9
Rural products	16	3.4
Base metals and their products	7.7	8.4

Taking into account that the import volume is higher than exports' (about 4.2 times) and the above ratios, it is easily concluded that the consumer price performance by international market means Albania's benefit on the side of import.

Trade - a lag in the world economy will mean decrease of the export demand and increase of trading costs in the developing countries. The most expected countries to suffer from these phenomena are countries with developed trade transactions that are remote from the markets where they export. The increase of the trading costs comes from higher c.i.f., due to higher risk perceived.

Albania's trade balance is largely conditioned by the trade transactions with the EU, with which Albania carries about 77 percent of imports and 93 percent of exports⁶.

Talking about an economic lag, the first idea striking your mind is the reduction of our partners' domestic demand for goods imported from Albania.

The following table presents the performance of Albanian exports to the EU countries during the first nine-month period of 2001:

Table 4 Performance of exports with the EU countries, year 2001

Year 2000	Exports in billions of Leks	Change in % (y/y)
January	3,046	27
February	3,811	20
March	3,832	36
April	3,726	45
May	3,684	21
June	3,625	0
July	2,453	-26
August	1,960	-9
September	3,486	12

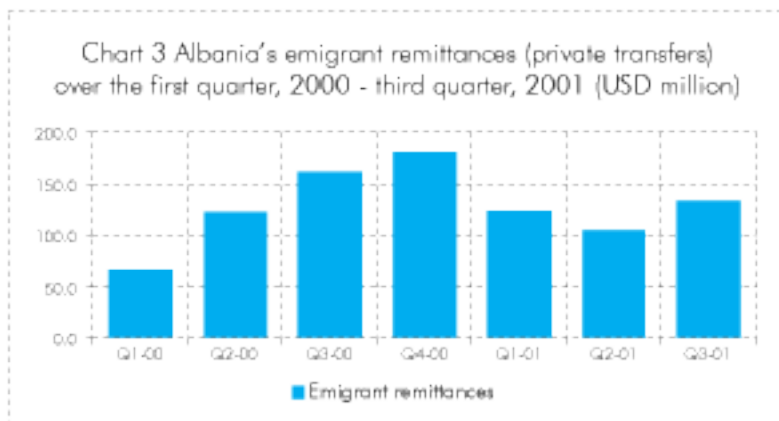
The year on year comparison is made to evidence the explanation of the core performance of seasonality phenomenon. Thus, it is evidenced that in June, July and August of 2001, Albanian exports to EU countries (mainly to Italy, Greece, Germany) have suffered a noticeable decline compared to these country exports of the previous year. With higher exports than in the previous year, September of the current year lags behind the growing rate of exports throughout the first months of the year. However one month is insufficient for jumping to conclusions.

Whether September exports stay at current rates or are lower, it might be said to a certain extent that import countries for goods made in Albania are passing a period of a downward demand for consumer goods.

It is understandable that the reduction of exports' rate compared to that of imports is not evidenced as a positive development for the current account and the balance of payments of Albania.

Emigrant remittances: Economic lag, frequently reflected in decreased work positions until now has been expected to influence on emigrant remittances. Jordan, Morocco, Tunisia that receive emigrant remittances from Central America and Western Europe, and some poor countries of Africa that benefit from emigrant remittances from USA are the countries to more meet with the decrease of emigrant remittances. Albania, whose

current account records about 36.6 percent of the income⁷ from emigrant remittances, has emigrants in both, the Western Europe and the USA.



F. EMIGRANT REMITTANCES

In addition to the first quarter that discloses increase compared to the first quarter of the previous year, the other two quarters give the impression that the world crisis has also touched the emigrant remittances. The second quarter is at 10 percent lower than in the previous year, while the third quarter is 20 percent. If the third quarter, usually marking the peak of emigrant remittances (on the occasion of year-end holidays) is considerably lower than that of the previous year, then we must almost surely say that one of the robust items of Albania's current account is shrinking because of the world crises⁸. However, during the fourth quarter of the current year, we must prepare to see changes because of Euro introduction.

G. ENDING NOTE

Recently, the frequently met saying through economic newspapers and magazines is that "Starting from September 11, the world is not the same". While the terrorist attacks hit

only USA; the effects are expected to fall on the whole world. A fact making you believe that forecast is the almost synchronized economic performance of USA, Europe and Japan during the first half of 2001. The instantaneous economic lag in USA and Europe, the weakening of information and technology sector, the crisis in Japan and the deterioration of new markets' financial conditions confirmed more robust global relations than thought before 2001. In order to analyze the reaction of the economy immediately after the terrorist attacks of 11 September, the provided examples were many natural disasters.

However, it must be admitted that the indirect effects of September 11 would have been more different and perhaps more serious than those caused by the natural disasters.

As expected, in the first weeks following the attack, the first negative reaction appeared in the form of reduced customer confidence and private expenditures in USA, weakened business trust either in Europe or USA and increased insecurity perceived by measures worldwide.

However, economists base their forecasts on some strong points for a somewhat more optimistic future than the current year. First, major economies took adequate support that was stronger than expected from their respective governments. It's worth mentioning the measures taken from the United States government to increase the government expenditures by USD 45 million (from which USD 40 million were only to recover the damage caused by the September 11 attacks) and the projections on curtailing taxes in year 2002. These reductions are expected to amount to -1.6 percent of GDP⁹. Second, the economic basis worldwide is more robust than those of some previous years ago. These bases are reflected in lower inflation rates, stronger fiscal positions, more flexible exchange rate regimes and lower sensitivity of developing markets externally. Third, the terrorist attacks are not expected to considerably change the increase of the USA productivity. The recent events however indicated that the crises could do much more harm to the economy, when they find it at a moment of lag.

NOTES

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¹ Cool Nerves at the Central Banks”, Financial Times, October 1, 2001.

² By definition, Albania falls under the group of “transition countries - Central and Eastern European countries and Former USSR countries”, but in the current analysis ‘developing and transition countries’ appear as a single group against the group of ‘developed countries’.

³ From the balance of payments viewpoint, foreign citizens not living in Albania and non-resident Albanians are considered the same, however, the division in this paper is as to the differences that both these traveller categories bear in the way of perceiving the country of residence.

⁴ Source: World Bank Report “On the recent event in low and middle income countries.

⁵ Source: Bank of Albania Statistical report data for 2000.

⁶ The same source, data for 2000.

⁷ Source: Bank of Albania Statistical Report data on year 2000.

⁸ Private transfers (nearly USD 530 million for year 2000) mostly serve to offset Albania’s trade deficit (about USD 820 million).

⁹ Source: HSBC Strategies on US fixed income, October 2001.