CHAPTER 4
ECONOMIC STRATEGY IN THE WAR ON TERRORISM:

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Introduction. On September 11, 2001 the United States faced a national security disaster. The attacks on New York City and the Pentagon snapped the nation into immediate action:

- Military forces were mobilized,
- President George W. Bush created an Office of Homeland Security, and
- Congress passed several pieces of legislation that were directly related to a global war on terrorism.

Economic Response. A crucial element of the federal government's action was the immediate call for economic assistance to local municipalities, businesses, national, and international actors.

- The economic assistance arising from the 9-11 attacks and subsequent military and political actions provide an interesting case for the study of the economic instrument of power.
- This paper traces the immediate actions that were taken by national leaders in an attempt to head off financial disaster in light of the 9-11 attacks and the subsequent call for a war against terrorism.

Economic Instruments of Power. The U.S. government (USG) can call on several instruments of power to ensure a particular national interest is achieved or a specific objective met.

- The military instrument of power is addressed in other publications.
- The dissemination of information serves as a key instrument for mobilizing resources in an open society. Watching CNN or reading newspapers helps to activate individuals and organizations alike.
- This paper discusses the economic instrument of power in response to 9-11.

Why Strategy is Difficult. In formulating a successful strategy to win the war on terrorism, We must carefully consider the right mix of military, political, informational, and economic instruments of power. Unfortunately, this is no easy task. Colin Gray—in explaining why strategy is difficult—frequently says that to tackle the fog and friction of war is akin to exploring unknown terrain.[2]

Similarly, Clausewitz argues that the key judgment that a statesman and commander must make is the kind of war he is fighting, not mistaking it for something alien to its nature.[3] President Bush is well aware of this Clausewitzian challenge in addressing the war on terrorism. President Bush says,

"It's a different type of battle. It's a different type of battlefield. It's a different type of war and that, in itself, is going to be a real challenge for America."

In short, making the strategic call in war is no easy task. Making that call is equally difficult when applying the economic instrument of power in this new war on terrorism.

- Forecasting economic effects, taking the appropriate measures, considering the right timing, and measuring the impact of economic actions are very difficult.
- Additionally, since economic actions do not occur in a vacuum, the sensitivity to international events on domestic financial and economic activities has grown greatly.
- The dynamic conditions that affect the economy are difficult to predict, let alone control.

Three Economic Issues. Since 9-11, the United States is facing economic issues on at least three fronts:

- Reconstruction. First, the most visible need for immediate economic aid is to help New York City. Requirements to expand homeland security measures from state and local governments also drive additional support requests throughout the nation.
- Fighting Recession. Second, national economic concerns are also being addressed to mitigate a general economic slowdown that had begun before 9-11, but has accelerated since the terrorist strikes. Airlines and insurance companies have requested loan guarantees or grants to avert possible bankruptcy. Similarly,

consumer and business confidence fell, which fanned recession.

- Economic Diplomacy. Third, the United States is taking international actions to:

  a) Help the United States and our allies and friends, and
  b) To immediately attack terrorist foes.

Washington had to calm world markets and ensure the free flow of international trade and finance. The U.S. reliance on coalition members and non-state actors to support a global assault on terrorism also required resources.

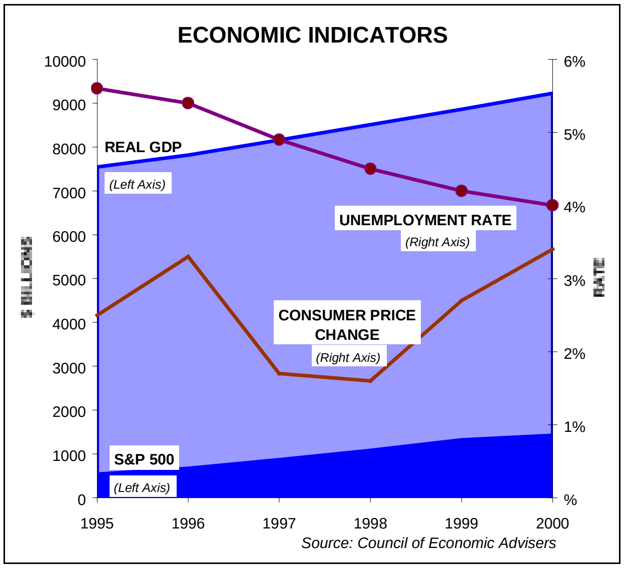
- The United States blocked terrorist assets and withheld economic resources against countries that harbored terrorists.
- U.S. foreign aid helps strengthen friends in the war against terrorism.

Context: Economic Slowdown

U.S. Economic Boom. Over the past year, the U.S. economy has been in the midst of transition from record high levels of economic activity to the current recession.

- From the mid-1990s to early 2000, the U.S. economy made tremendous gains. Gross domestic product (GDP), unemployment, inflation, and stock market performance indicated that the American economy was on the upswing. (See Figure 4-A.)
- The nation's GDP was experiencing real growth at a very healthy rate as high technology industries related to information technologies and bio-technology firms led the charge.
- Increased productivity among workers, partly caused by increased automation and information access, boosted GDP, as businesses were able to produce more goods and services for both domestic and international markets. Potential rates of economic growth were buoyed with increased productivity among American workers and businesses.
- This growth was manifested by very low unemployment rates through 2000.
- Individuals who invested in the stock market could not help but to increase the value of their portfolios. The S&P 500 Index almost tripled in value within this period.

Figure 4-A Economic Indicators



U.S. Economic Slowdown. By August 2001, the economy was still strong, but was showing signs of fatigue and stress.

- By the second quarter of 2001 real GDP had grown by a miniscule 0.3% compared to a similar period in 2000 at 1.3%.
- The unemployment rates rose to 4.9%. About 6.9M American were without jobs, in comparison to 5.5M a year before.
- Consumer prices were also rising to 3.7%.
- Firms that had increased their high tech investments by 20% per year from 1996 to 2000 began to cut back on such purchases at the point where they saw only marginal gains in productivity.[4]
- As businesses started to reduce their investment in high tech and information systems, firms that sold computer, communications, and information goods and services faced fewer opportunities and "downsized" their operations.
- Many supporting industrial sectors and services also fell like dominoes as firms pulled the plug on the information industry.
- Foreign suppliers also suffered and their earnings fell—which in turn reduced their ability to import American goods.
- Additionally, energy prices for oil, natural gas, and electricity were increasing by late

2000—thereby weakening businesses' financial position.

- State and local governments (notably California) were forced to subsidize utilities and support higher unemployment claims. They watched helplessly as budget surpluses melted into pools of red ink.

Stocks Fall. Stock markets were another victim of the economy's cooling.

- The S&P 500 Index dropped to 1,092.54 at the close of business on September 10, 2001 from its 2000 year-end closing of 1,427.22 points.
- The reduction in stock prices—due to reduced profits of high tech and other firms—caused the cost of capital to rise.
- Firms faced with decreased profits were forced to pay more for loans and to cut unprofitable operations, resulting in further unemployment.
- Consumers—seeing their wealth reduced—delayed or cancelled spending on items ranging from luxury items to ordinary goods and services.

Budget Woes. The federal, state, and local governments were not immune to the economic decline either.

- Decreased economic activity translated into reduced tax revenue and calls for increased, unexpected unemployment and social assistance to laid-off workers.
- The federal government's projections of a growing budget surplus vanished and deficit reduction efforts were delayed. The government could try to raise taxes, further reduce spending, or borrow funds—alternatives that all had serious economic consequences.

Slowdown. The economic downturn was not an American phenomenon either.

- The U.S. economy that was fueled by the globalization of free market ideas and access was now reeling as many nations' economies contracted.
- As the U.S. economy faltered, American consumers reduced purchases of foreign goods and services.
- Already shaken, Asian and European economies decelerated more rapidly.

General Response. In response to faltering GDP, the USG has a number of ways to boost aggregate demand.

- To close the aggregate demand shortfall, more spending must take somewhere.
- The USG can make it easier for consumers and businesses to spend money. This is done via tax cuts or cuts in interest rates.
- But if consumers and businesses lose the confidence or ability to spend money, the USG must have the confidence to spend enough money to close the shortfall of aggregate demand.

Fiscal Response. In response to the faltering economy, President Bush attempted several measures to alleviate the problem.

- Bush introduced measures to immediately increase consumer spending by reducing income tax rates in several areas and introducing tax rebates that were sent to households in the summer of 2001.
- Since consumption represents about two thirds of the nation's GDP, getting people to purchase goods and services in light of decreased economic activity was paramount.
- Higher demand for goods and services would maintain or even increase production, reduce unemployment, and steady the nation.

Economists debated the costs and benefits to society of cutting taxes and issuing rebate checks instead of reducing the surplus despite the worsening economy.

- The Bush administration's answer was not to increase overall federal government spending, but to focus on business and markets to create solutions.

Monetary Response. Similarly, the Federal Reserve System (Fed), tried to stem the tide:

- The Fed started to reduce the federal funds rate (the interest rate that commercial banks lend to one another overnight) in order to increase the amount of money in the economy.

The Fed's hope was to encourage investment by businesses and avoid a recession. These economic problems seemed to persist as the stock markets slid further and consumer confidence waned. Greenspan had increased interest rates just a year before to stave off a potential rise in inflation.

- Some critics have argued that the Fed's rise in interest rates contributed to the reduction in business investment that resulted in the slowdown in 2001.
- Conversely, some observers noted that the Federal Reserve System's continued rate reductions were having little immediate relief for the economic future.

In any event, the Fed engineered a program to cut the federal funds rate in half.

- For example, the federal discount rate (the rate that the federal government charges to banks) dropped from 6.0% to 3.0% from September 2000 to 2001.
- Commercial banks followed suit during the same period by reducing the prime rate (interest rates charged by banks to their best customers) from a high of 9.5% to about 6.5%.

Response Frustration. Unfortunately, nothing seemed to work. The economy was in decline, not simply experiencing temporarily weak or below average returns. The economy was sliding towards a recession.

- Investment was not rising.
- Manufacturers continued to lay-off workers and employment opportunities decreased.
- Income, sales, and production declined.

Crisis Strikes

Impact of 9-11. On September 11, 2001 two airliners struck and destroyed the World Trade Center Twin Towers in lower Manhattan that immediately disrupted the U.S. economy. Although another plane hit the Pentagon with a tremendous loss of life, it did not have the same economic impact of the New York attack. The combined attacks caused over 3,000 deaths and devastated the nation.

Striking the financial center of the United States and the world dealt a severe blow to a struggling U.S. economy.

- 9-11 hit world financial markets, investment banking, direct corporate operations, and equity and debt markets.
- It shattered the confidence of business and consumer alike.

NYC Reconstruction. In addition, New York City had to address the staggering costs of replacing the destroyed infrastructure.[5]

- On October 4, 2001 New York City Comptroller Alan G. Hevesi estimated that the city had suffered about $34B in property damage.
- Other estimates for the national attack skyrocketed to $75B. The city alone lost 13M square feet of office space—equal to the commercial office space of Atlanta.
- If one considers damaged areas too, more than 30M square feet of office space was affected.

Although one cannot replace the value of human life, the attacked resulted in a loss of "human capital" of $11B from the productive capacity of the lost lives.

- For example, New York employs a significant portion of the nation's security investment, advertising, and book publishing workforce.
- Before the attacks, the financial services industry employed well over 522,000 workers, making it the biggest industry within New York City.
- About $207.5B of an annual city income of $444.4B was related to this sector.
- Tourism, another New York staple, was another casualty as people stayed away from the city.

Wall Street Woes. Fixing New York's problems, however, was not the only concern that national leaders considered while economic paralysis spread across America.

- Not only did consumer confidence sink, but also the New York Stock Exchange and other exchanges were closed for six days. The halted trading in securities added to heightened anxiety.
- Many of the firms located in the World Trade Center Twin Towers were directly involved in securities trading, but amazingly

the stock exchanges did operate, despite a fall of 7% in value on the opening day of trading.[6]
- Similarly, the disruption of airline services due to the fear of further attacks, increased security, public fear, and lawsuits that could drag many firms into bankruptcy.
- Additionally, major insurers could make the World Trade Center attack the most costly in history—threatening the financial viability of many insurers. Insurers would also need to raise more reserves and could do so by raising premiums—complicating industries that were already struggling to cut costs and boost profits.

American and foreign investors did not know the extent of the damages to the various stock, bond, and commodity exchanges in New York City. Access to communications, data, records, and securities traders were questionable after the destruction of the World Trade Center Twin Towers. Additionally, other buildings were damaged and many persons and businesses involved in the investment markets were without offices. Fear from further attacks in the lower Manhattan area also closed off many areas in the city. Fortunately, these concerns ebbed as solutions were found to operate the stock and other markets, albeit a few days later.

Airline Angst. Several airlines were already facing financial ruin before 9-11.

- Although United and American Airlines had both lost two aircraft each during the attack, the entire airline industry sputtered.
- The industry suffered from declining bookings of business travel, because of the general downturn in the economy throughout the summer.
- Additionally, increased labor and fuel costs had reduced further profits. Industry analysts had estimated that the airlines would lose $3.5B in 2001 before the attacks, with United Airlines losing $1B alone.[7]
- Airlines would have to brace for a host of new federal security measures, loss in passenger confidence, and lawsuits filed in conjunction with the attacks.
- Major carriers reduced the number of scheduled flights by 20% and saw flights filled at less than 50% on most routes one week after the airlines were permitted to restore services.
- Airlines close to the brink of financial ruin could declare bankruptcy and spark turmoil in the transportation industry.
- By September 17, the airline industry and Boeing, the sole United States manufacturer of major airline aircraft, had laid off 70,000 employees.
- Additionally, reduced airline services also affected tourism throughout the United States, shocking California and Hawaii, who, despite being a continent away from the East Coast, suffered large losses of tourism.

Insurers Hit. 9-11 also hammered the insurance industry.

- Insurers at and near the World Trade Center faced a host of claims from individuals, businesses, and building owners in terms of property and casualty, health care costs, worker's compensation, lawsuits against the airlines, and the prospects of rising premiums that might force the insured to find new alternatives.
- Insurance companies also face a problem with policies that protect firms from the interruption of normal activities. (Most firms purchase a policy that covers an interruption of normal business because of a catastrophe.)
- Thousands of businesses around the nation were affected from firms that were unable to communicate with New York offices or with those who trade on the stock market or sell commodities.

These claims will force insurance companies to raise premiums that will be born on the shoulders of business and individuals.

- For example, insurers started to increase a host of premiums on a variety of policies since the record payments made to the victims of Hurricane Andrew in 1992—when the industry paid out claims of about $16B.

- Insurance premiums for the Miami area and Florida were boosted 250% and 110% respectively.

In light of these record payments, insurers started to diversify risk by using reinsurers.

- Reinsurers, who take a portion of the insurance liability from a policy writer, may default because of the magnitude of the attack.
- Major insurance firms that relied on these reinsurers may need to pay off claim amounts that were unanticipated.
- Many small insurers or firms that were involved in commercial property insurance face financial disaster given the virtual size of potential claims from New York, the other airline crashes, and other affects.

Shock to Aggregate Demand. The United States also faced a macroeconomic problem due to the terrorist-induced crisis. In essence, the U.S. economy faced a shortage of aggregate demand.

- Demand declined not only from the multiplier effects as supporting industries lost opportunities across the economy, but also
- There was a decline in demand due to a general malaise of consumer and business confidence in the face of such inhumane barbarism and attacks on basic freedoms.

Crisis Response

Policy Questions. Thus, a number of microeconomic and macroeconomic policy challenges confronted the government while also facing an immediate crisis. What steps should the government take? Clearly, the government would want to get the American economy back into operation. However, many policy questions remained unanswered.

- Should the government purposely support or subsidize industries that were damaged by the attack?
  - By their nature, insurance companies assume risk for disaster at a price that often excludes government subsidies.
- If the government declared the attacks as "an act of war," then would those firms be relieved of any legal liability?
- Does the government set a precedent by supporting industries whenever there are catastrophic events?
- Or should it limit its economic actions towards improving the general economy and letting the free market decide who survives?
- How should the government become involved in the running of the economy?
- What actions can and should the government take against any attackers?

USG Response. The United States economy seemed paralyzed after the attack.

- Uncertainty, fear, lack of communications, and other concerns slowed business activities in New York and around the country.
- Airline flights were grounded, stock trading halted, financial transactions delayed, and the federal government re-focused on the immediate attack.

In response, the USG took three major actions.

- First, the federal government moved quickly towards fiscal policy to provide funding for programs ranging from humanitarian aid to increased military spending.
- Second, monetary policy was used to increase the money supply to assure that financial institutions, businesses, and individuals could conduct transactions.
- Third, the government took actions in the international arena to support a coalition against terrorism and reduce the ability of certain actors to use financial resources.

These elements of economic power were tools that the government could use to achieve certain national interests: maintaining economic viability and national security.

Fiscal Policy

Funding Issues. The United States government faced several diverse economic issues in the wake of the 9-11 attacks.

- Calls for immediate homeland security and military action require additional funding for equipment, personnel, and operations.

- Not only were immediate actions required to secure airports and New York City, but preparing military personnel and equipment to deploy to particular theaters for an indefinite time period requires sustained budget increases.
- Since operations against terrorist organizations might involve Middle Eastern access to oil, some advocates of the domestic energy industry wanted government support to expand energy sources for the country.

Key Questions: These actions require national leadership to decide:

- How much to spend,
- How long it should last,
- Who gets funding, and
- How the nation will pay for these actions.

Key Funding Options. The government has several possibilities to fund programs:

- Raise taxes, borrow funds, change funding priorities,
- Divert surplus funds,
- Shift responsibilities for programs from the federal government to other actors.
- Additionally, the government could try to establish a proper environment to rebuild the economy.

Financing Options. The federal government can finance additional expenditures through increased taxes, reprogrammed activities, payments from a budget surplus, or via borrowing actions. But given the grim economic conditions in the U.S. and global economy, some of these options were non-starters.

- For instance, raising taxes would only reduce aggregate demand, worsen the recession, and fan rising unemployment.
- Additionally, Bush and the Congress had already passed a tax reduction program that summer. Likewise, existing programs were not touched.
- The government has fewer discretionary programs to reduce. The one major program left was defense, which would have to be increased to fight terrorism and secure the nation.
- The only other source was the surplus for the fiscal year. Instead of retiring the federal debt earlier, the government would continue to pay interest on the debt by using the surplus.
- Unfortunately, tax revenues that made the surplus possible would probably decline because of the economic slowdown in individual and business income and declining import tariffs—a double hit.

Tax Cut Program. Before the New York and Pentagon attacks, the Congress approved and President Bush signed a $1.35 trillion tax reduction program into law in June 2001. But many legislators were leery about the cuts. Why?

- One of the concerns about such a hefty tax cut involved its impact on the budget surplus. In 2000, the federal government was straddled with a $5.6 trillion debt.

Although the federal government had surplus budgets since 1998, the source of the surplus was excess Social Security and other retirement program tax receipts. (In 2000 the excess was about $253.5B.)

- Many Democratic members of Congress were concerned that these tax cuts would be financed by the Social Security surplus alone.

The Bush administration and Congress made an agreement to use the Social Security surplus to only pay-off the debt by putting the funds in a "lockbox."

- This lockbox was a restraint for policymakers to limit tax or spending initiatives to combat the sliding economy.

Supplementary Spending Items. Right after the attacks, President Bush requested emergency spending authority and appropriations for disaster relief, military operations, and to fight the war on terrorism.

- The House of Representatives and the Senate unanimously approved a $40B supplemental spending bill on September 14.
- The Social Security lock-box was broken. Bush released $5.1B on September 21.

- Approximately $2.5B went to the Department of Defense to upgrade intelligence and security, readiness, force protection, and repair the Pentagon.
- Another $2B was allocated to the Federal Emergency Management Agency for debris removal, individual and family assistance, disaster aid, and other support in New York and other affected areas.[8]

President Bush received discretionary authority to spend $20B for post 9-11 programs.

- Congress then appropriated an additional $15B to support the airlines. The $15B funding for the airlines included $5B in cash and $10B in loan guarantees. The airlines had asked for $24B.
- President Bush also requested $18.4B for more defense spending and $8.3 for ballistic missile defense programs from the Congress.

Ramping Up Government Spending. Some of the increased government spending will be temporary, but other amounts may create a larger, more permanent addition to the government. For example:

- Proposals to make airport security personnel federal employees would certainly add to the federal government bureaucracy.
- Other "automatic stabilizers," e.g., welfare and food stamp programs, would also rise due to additional lay-offs during a slowing economy. For example, a part of the government's fiscal stimulus also included an enhanced unemployment insurance program that extended coverage for unemployed workers from 26-weeks to 39-weeks.

Fiscal Stimulus. In response to clear signs that 9-11 was accelerating the plunge of the U.S. economy into a recession, additional calls were made for a greater economic stimulus program.

- In early October, President Bush requested an additional fiscal stimulus of $60B-$75B.
- The Senate Majority Leader Tom Daschle proposed one of $50B.

Depending on which version one examines, the emphasis to improve the economy has wide-ranging policy implications.

- President Bush's proposal included capital-gains tax cuts and increased depreciation write-offs on capital equipment.
- Democrats wanted a rise in the minimum wage.

These proposals were debated well before the 9-11 attacks by each respective camp. Some critics questioned whether each party was using the current economic downturn and emotions of the 9-11 events to pass long-held party positions and economic objectives.

Monetary Policy

Looser Monetary Policy. Monetary policy was another tool available to the federal government to alter economic conditions. The Fed went into action immediately after the attacks. He realized that worldwide financial uncertainty about the economic future could cause a global retreat on a number of economic fronts: banking, consumer, investment, and business confidence might plunge and worsen the damage to the United States' economy.

- The Fed immediately ordered the purchase of federal government bonds that pushed excess money into the hands of securities traders and investors.
- On September 14, the Fed bought $80B worth of U.S. Treasury securities on the open market and a further $57B on September 17.
- The Fed also made an additional $11.7B available for loans to banks.
- In addition, the Fed made an arrangement with the European Central Bank (along with separate arrangements with other foreign banks) to ensure that it would guarantee up to $50B in currency exchanges to support foreign bank operations in the United States. Interest rates dropped fast.

The Fed was trying to boost consumer confidence and make sure that money was available for financial transactions to stabilize economic activities. The Fed also started to lower the discount rate and the federal funds rate. These sensitive rates were immediate signals that the government would take action to stem the economic downturn.

- The federal funds rate had stood at 3.5% on September 10 and dropped as low as 1.25% on the September 18.[9]
- By late October, the rate stabilized to around 2.5%. The discount rate dropped from 3.0% on September 10 to 2.0% on October 26.
- These low interest rates, if one calculated the effective inflation rate, made the cost of borrowing almost negligible.
- Longer-term interest rates also fell, but not as dramatically.

Admittedly, encouraging business and individual borrowing is a long term process, but calming markets and consumers confidence is an important objective for the FED.

- Lower interest rates may have an effect on consumer behavior by reducing savings.
- As interest rates fall, returns on interest bearing securities such as passbook savings accounts or certificates of deposit have less appeal to individuals. They can invest in stocks, real estate, or other instruments for higher returns.
- Conversely, they may feel like they might as well purchase goods and services since savings provide lower future returns.

Natural Disaster Parallel. Except for the increased military and security spending, the U.S. response to the destruction of the World Trade Center Twin Towers and the Pentagon were generally treated as if the events were like a natural disaster.

- Earthquakes or floods can damage or destroy whole cities or regions.
- Fiscal stimulus can provide instant financial support for those communities.
- Monetary policy is usually used for national level economic concerns.

The difference between the 9-11 attacks and a natural disaster was the scope of the attack and the threat to the nation.

- The New York and Washington attacks had far reaching domestic and international impacts.
- National leadership was needed to wield the economic instrument of power to avert a further worldwide economic downturn.
- Additionally, steps were taken to reduce the apparent terrorist threat on an international level.

International Policy

Economic Sanctions. A common economic tool used against a nation-state or non-state actor is sanctions. Sanctions attempt to curtail or limit access or the benefit of trade or financial resources. Cutting off financial assets to 27 terrorist groups was a first step to limit or make support difficult for a terrorist network with no visible means of support.

Money and financial support is vital for terrorist groups.

- Financial resources allow terrorists to purchase equipment, travel, and live in targeted nations.
- Secretary of State Colin Powell observed that “money is the oxygen of terrorism.”[10]

President Bush instituted sanctions against Usama bin Laden, the *al Qaeda* terrorist group, and other groups through Executive Order 13224, "Blocking Property and Prohibiting Transactions With Persons Who Commit, or Support Terrorism" on September 24.[11]

- No United States citizen or person residing in the United States could make or receive any contribution of funds, goods, or services to or for the benefit of selected groups identified by the State and Treasury Departments.
- Additionally, no one in the United States could sell items to these groups or make donations.
- The Treasury Department was also allowed to take other actions such as disrupt the financial infrastructure of groups by freezing and blocking the use of assets held in the United States and coordinate actions with other countries to freeze or seize terrorist assets.

The Treasury Department created an interagency organization, the Foreign Terrorist Asset Tracking Center (FTATC), to observe and identify the source and uses of financial resources of terrorist groups.

- As of December 2001, treasury has blocked almost $70M in terrorist assets.[12]

No Easy Task. The large volume of typical banking transactions makes tracking and seizing terrorist funds difficult and expensive.

- The United States government must not only coordinate actions between law enforcement, federal banking regulators, the banking industry, and financial institutions.
- It must monitor international transactions.
- International banks and foreign governments have sought more evidence to seize financial assets.
- Additionally, ordinary citizens may question their invasion of privacy and banks may have to institute higher cost banking enforcement practices that will be paid by consumers and the banking industry.

UN Action. The United States had no need to take additional economic actions against the Taliban government in Afghanistan. In December 2000, the United Nations had passed Security Council Resolution 1333 that specifically targeted the Taliban since it harbored Usama bin Laden. United Nation members were directed to:

- Freeze bin Ladin's financial assets,
- Institute an arms embargo against the Taliban, and reduce their offices and missions presence overseas,
- Ban the export of equipment to make heroin, and
- Close all non-humanitarian assistance flights into and out of Afghanistan. [13]

These sanctions were not a total stoppage of goods and services to the Taliban. Private sector trade and commerce, humanitarian aid, and exemptions to avoid hurting the Afghan people were allowed.

Support to Pakistan. President Bush supported the lifting of sanctions placed on Pakistan when its government supported United States efforts to capture bin Laden and conduct military operations in Afghanistan. Sanctions were placed on Pakistan because it had detonated nuclear devices in 1998.

- The House of Representatives approved a two-year suspension on restrictions to economic aid for Pakistan in response to its efforts to help the United States.
- Along with lifting sanctions, the United States moved towards rescheduling up to $379M in government-to-government debt.
- Additionally, the United States urged the International Monetary Fund and the World Bank to provide loans and aid to Pakistan.
- These actions rewarded Pakistan's government for support of American and allied nations against terrorism and domestic opposition.

Closer Ties to Jordan. Pakistan was not the only country that was given economic support. The United States also garnered support from another Muslim country against the war on terrorism, Jordan.

- President Bush and the Congress agreed to a U.S.-Jordan Free Trade Agreement that would create investment opportunities for that region.
- This trade agreement was designed to "send a strong message to Jordan, as well as other countries in the region, that support for peace and economic reform yields concrete benefits."[14]
- Bush signed the agreement on September 28.
- Although there was no financial direct aid involved, the trade agreement was a clear signal that the United States intended to strengthen economic ties with Jordan.

More Foreign Assistance. The United States also used foreign assistance to support persons and states in economic need.

- U.S. humanitarian assistance to Afghanistan totaled $320M, while financial assistance was given to other countries, like Pakistan, to support Afghan refugees.
- The United States Government could also remove restrictions on and approve economic aid to nations that support American foreign policy initiatives.
- For example, on October 16, Secretary of State Colin Powell recommended to the

Senate Foreign Relations Committee that restrictions on financial aid on Azerbaijan be lifted.[15]

Conclusions

Economic Crisis Management. The United States had several tools available to contain a possible economic disaster and support a subsequent war on terrorism.

- Many of these tools were quickly used to stem a potential economic disaster in the United States and around the world.
- Additionally, some tools were used to support actions taken against terrorists and to complement military and political instruments in play.
- The economic instrument of power was able to take immediate action like freezing terrorist assets once they were identified or paying for additional security.

Longer Term Strategy. Other tools, however, are more long-term and complex. For instance:

- Stopping growing unemployment or slipping GDP growth for the world's largest economy in the world is no small order.
- For example, getting businesses to gather enough confidence to purchase new plant and equipment takes time.
- The government can provide some stimulus, but much of a country's economic growth needs to come from business and individuals.
- Fiscal and monetary policies help shape, but do not guarantee economic health.

Decisive Actions. Globalization has made economics a more valuable tool of influence around the world. The United States can and does take advantage of globalization by using its economic instrument of power as a flexible and powerful tool in achieving its goals in the war on terrorism.

- The application of economic instruments of power, in the case of the 9-11 attacks, was timely and aggressive.
- Actions were swift, decisive, and aimed at alleviating suffering, enabling operations, making structural changes, and soothing the psyche of domestic and international actors.

New Ties That Bind. Nations that did not have much in common in the past now have shared instruments with trade and economic growth.

- Financial markets and national economies are more integrated and sensitive about any action that can affect trade or finance.
- Stock markets around the world trade securities of foreign firms as commonly as their own domestic firms.
- Equity investments, trade ministers, and world business leaders have much at stake with their financial transactions at home and abroad.
- They are heavily affected by actions within the United States.

New U.S. Resolve. President Bush has expressed a new U.S. resolve to win the war on terrorism. "We will not tire. We will not falter. We will not fail." In addition to winning the war on terrorism, President Bush is determined to return the nation towards the path of economic recovery.

Endnotes

1 This chapter is adapted from a paper by Dr. Clay Chun, Professor of Economics at the U.S. Army War College and a member of CINCPAC's Economic Security Working Group.

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3 Carl von Clausewitz, *On War.*

4 Robert T. Parry, *FRBSF Economic Letter*, Federal Reserve Bank of San Francisco, July 6, 2001.

5 Peter Coy, The Center Must Hold" *Business Week*, October 22, 2001; Aravinf Adiga, et al "Sudden Impact," *Money*, November 2001; Lewis Braham, "On the Disabled List: New York" *BusinessWeek*, September 24, 2001.

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7 Michael Arndt and Lorraine Woellert, *BusinessWeek*, September 24, 2001 and October 1, 2001.

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