

TERRORISM & THE FINANCIAL MARKETS

By Dominic Lucente, CFP

Wall Street has the potential to recover quickly from geopolitical shocks.

In the past few months, the world has seen several high-profile terrorist attacks. Incidents in the U.S., Belgium, Pakistan, Lebanon, Russia, and France have claimed more than 500 lives and injured approximately 1,000 people. Beyond these incidents, many other deaths and injuries have been caused by terrorist bombings that garnered less media attention.^{1,2}

As an anxious world worries about the ongoing threat posed by ISIS, the Taliban, al-Qaeda, Boko Haram, and other terror groups, there is also concern about the effect of such incidents on global financial markets. Wall Street, which has had a trying first quarter, hopes that such shocks will not prompt downturns. Even in such instances, history suggests that any damage to global shares might be temporary.

While geopolitical shocks tend to scare bulls, the effect is usually short-term. On September 11, 2001, the attack on America occurred roughly at the beginning of the market day. U.S. financial markets immediately closed (as they were a potential target) and remained shuttered the rest of that trading week. When Wall Street reopened, stocks fell sharply; the S&P 500 lost 11.6% and the Nasdaq Composite 16.1% in the week of September 17-21, 2001. Even so, the market rebounded. By October 11, the S&P had returned to the level it was at prior to the tragedy, and it continued to rise for the next few months.^{3,4}

In the U.S., investors seemed only momentarily concerned by the March 11, 2004 Madrid train bombings. The S&P 500 fell 17.11 points on that day, as part of a descent that had begun earlier in the month; just a few trading days later, it had gained back what it had lost.⁵

Perhaps you recall the London Underground bombing of July 7, 2005. That terror attack occurred on a trading day, but U.K. investors were not rattled; the FTSE 100 closed higher on July 8 and gained 21% for the year.⁴

Wall Street is remarkably resilient. Institutional investors ride through many of these disruptions with remarkable assurance. Investors (especially overseas investors) have acknowledged the threat of terrorism for decades, also realizing that it does not ordinarily impact whole economies or alter market climates for any sustained length of time.

You could argue that the events of fall 2008 panicked U.S. investors perhaps more than any geopolitical event in this century: the credit crisis, the collapse of Lehman Bros. and the troubles of Fannie, Freddie, Merrill Lynch, and Bear Stearns snowballed to encourage the worst bear market in recent times.

When Hurricane Katrina hit in 2005, truly devastating New Orleans and impacting the whole Gulf Coast, it was the costliest natural disaster in the history of the nation. It did \$108 billion in damage and took more than 1,200 lives. Yet on the day it slammed ashore, U.S. stocks rose 0.6% while global stocks were flat.^{4,6}

The recent terror attacks in

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Belgium, Pakistan, and France have stunned us. Attacks like these can stun the financial markets as well, but the markets are capable of rebounding from their initial reaction.

Dominic Lucente may be reached at 603.645.8131 or dominic.lucente@lpl.com. dlucente.com

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Citations.

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