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AFTER PARIS: NOTES ON THE ECONOMIC IMPACT

Berenberg Macro Flash

We bow our heads to the victims of terror. Our thoughts and prayers are with the victims and their families and friends.

In the wake of such heinous criminal acts, economic considerations take a back seat. Still, as economists, we have to ask what the economic impact may be.

Experience suggests that such acts of terror do not derail economic trends in mature Western economies.

- After the 7 July 2005 bomb explosions in **London**, UK private consumption rose 0.7% qoq in Q3 2005, in line with the average of the previous 4 quarters.
- After the 11 March 2004 attack near **Madrid's** Atocha train station, Spanish consumption growth rose to Q2 2004 to 1.2% qoq after a Q1 dip to 0.6% qoq before returning to the previous trend thereafter.
- In the US, consumer spending briefly accelerated after the 9/11 2001 terror attacks to 1.5% qoq in Q4 2001 followed by an offsetting dip to just 0.3% qoq in Q1 2002.

The response to the terrible terror attacks in Paris will likely mean additional public spending on police and the military, but probably not to such an extent as to make a major difference to short-term aggregate demand. At the margin, the need to react to the serious challenge may lead to slightly larger fiscal deficits and to a greater political acceptance of small deficit overshoots on the European level.

Of course, the terror attacks raise profound political issues that can also have longer-term economic consequences. While difficult and potentially contentious decisions are ahead, the external threat can also serve as reminder of the ties that bind Europe and its citizens and nations together. We can only phrase the issues as questions rather than as putative answers.

- Both Russia and the West have been hit by heinous acts of apparent Islamist terror within a few days. Will the major powers now try to sort out the Syrian problem much more energetically, as the tentative progress at the last talks on Syria and first reports from the G20 may suggest?
- Will the political fallout from the terror attacks make it easier or more difficult to tackle other urgent issues such as the refugee crisis?
- While right-wing populists may try to use the attacks to their political advantage, could the violent challenge to the civilized world also make it easier for the mainstream parties in Europe to set some of their differences aside and work together more closely, including on attempts to do more to integrate refugees? Or will it detract from the need for reforms, for instance from the labour market reforms needed to ease the integration of migrants, refugees and long-term unemployed into the labour market?

The **long-term economic impact** is difficult to judge. A lot will depend how forceful the West now reacts to the challenge. Near-term, we do not expect any significant break to the established economic trends in Europe, that is to a mediocre economic upswing led mostly by private consumption. We look for Eurozone growth to return to its 1.7% trend over the course of 2016 after a dip in 2H 2015 caused by declining exports to some major emerging markets.



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