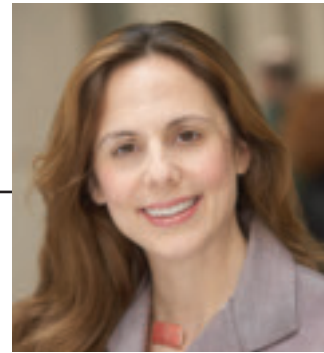


Shock Value

Coming to terms with the market impact of terrorist attacks.

EDITORIAL



How can you begin to measure the costs of a terrorist attack? When lives are lost and communities badly damaged, it seems almost callous to talk about economic value. But since Sept. 11th, 2001, governments worldwide have been trying to put in place contingency plans and, in particular, mechanisms to help firms deal with the overwhelming costs of rebuilding businesses lost to such disasters. Last December, for example, U.S. President George Bush extended the Terrorism Risk Insurance Act to the end of 2007 to help ensure U.S. firms have adequate insurance coverage in the event of a terrorist attack.

While these attacks are a risk to people and the communities they live in, to a firm's shareholders, they are also a major risk to value. And to the plan sponsors responsible for managing the retirement savings of Canadians, it's a risk they can't ignore. Yet few comprehensive studies have been done that actually link the impact of terrorism to financial markets and firms—until now. A recent study, conducted by Andrew Karolyi and Rodolfo Martell, shines a light on the extent to which such attacks affect shareholder value. The pair looked at 75 terrorist incidents worldwide from 1995 to 2002 and found these resulted in an average loss in stock value of US\$401 million per incident. Moreover, they found that target companies saw their stock prices drop an average of 0.83% on the day of each

attack. And the situation fails to improve after that, according to Karolyi and Martell. In the days and weeks that follow, while such companies don't continue to lose stock value, they don't regain it either.

In this issue of *Canadian Investment Review*, Karolyi points out the gaps in research and takes a look at what we do and don't know about terrorism and value. His analysis has important implications for sponsors. Whether or not a company is at risk of a terrorist attack should matter for investors, he points out. So having the right research to consult is critical.

On another note, I'd like to draw your attention to a new column by John Ilkiw. You might have noticed it in the Spring issue when he turned his attention to the history of options. This month, Ilkiw takes a look at alpha and beta to find out exactly where these terms came from and how they came to be so widely used in the lexicon of financial management. We hope you'll enjoy this and his other columns in the issues to come. ■ —Caroline Cakebread

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