

Terrorism and its Impact on Financial Performance: A Case of Tourism Industry

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Abstract

Tourism has emerged as an instrument for generating substantial economic benefits to both host countries and tourists' home countries. It is an especially important industry for the developing economies. The main benefits of tourism to a country are foreign exchange earnings, tax revenues, and business opportunities for entrepreneurs, and employment generation for workers, poverty alleviation and sustainable human development in the industry. But the free flow of information, communication, information technology and so forth has posed an open challenge to the tourism industry, since the terrorist groups are conducting their activities by seeking benefits from these developments, and hence affecting the countries globally. The fear of terrorism is growing large in our daily life. There are a number of supporting case studies where these terrorist attacks have caused a number of problems for tourist activity in a country including India. The present paper evaluates the impact of financial performance on the tourism industry in India. Various studies have been done to measure the magnitude of the effect of an unanticipated event. The present paper studies the impact of an unanticipated event i.e., the 2008 Mumbai attacks (sometimes referred to as 26/11) on the financial performance of tourism industry. The study examines the effect of this unanticipated event on the balance sheets of the India Tourism Development Corporation (ITDC) which is the only Public Sector Undertaking of the Ministry of Tourism. To study the impact, the financial statements of ITDC from the financial year March 2006 to March 2010 is evaluated. The key figures such as liquidity ratios, leverage ratios, per share ratios, profitability ratios, and direct foreign exchange earnings are evaluated. The Paired T-test is applied to check the impact on the financial performance of the tourism department before and after the attack. Impact of terror attack is visible on the financial performance of the tourism industry. The decrease in the performance clearly indicates the impact of terrorism in the tourism sector.

Keywords: financial performance, terrorism, tourism, Paired T-test.

JEL Classification: G30, G34, L25

I. Introduction

Tourism has emerged as an instrument for generating substantial economic benefits to both host countries and tourists' home countries. It is an especially important industry to developing countries. The main benefits of tourism to a country are foreign exchange earnings, tax revenues, and business opportunities for entrepreneurs, and employment generation for workers, poverty alleviation and sustainable human development in the industry. According to the World Tourism Organization (WTO), "Tourism is one of the top five export categories for as many as 83% of countries and is the main source of foreign exchange earnings for at least 38% of countries." But the free flow of information, communication, information technology and so forth has posed an open challenge to the tourism industry since the terrorist groups are conducting their activities by seeking benefits from these developments, and hence affecting the countries globally. The fear of terrorism is growing large in our daily life. There are a number of supporting case studies where these terrorist attacks have caused several problems for tourist activity in a country including India.

Terrorists choose to attack tourists as opposed to the citizens of the host countries. It is because the tourists are easy to talk. Besides, attacking the international tourists generates the great deal of fear among the tourists which causes the tourists to avoid travelling to that part of the world. Moreover, the terrorists themselves stay in the local part of the host country and hence the local people knows them and does not deliver any information to them.

Tourism contributes to the economic development and is the major source of revenue generation for any economy. But this relationship exists when the positive global conditions exists. When the conditions like terrorism

exist, its impact is enormous (Essner, 2003). The negative conditions like terrorism, not only affects the tourism industry but the economy as a whole. The repercussions of terrorism extend beyond activities that are directly associated with tourism, notably airlines, hotels and catering and to sectors that supply intermediate or final goods that are purchased by firms and employees in the industry, so that all sectors of the economy are affected to a greater or lesser extent (Blake and Sinclair, 2002).

According to the World Tourism Organization (WTO), international tourism generated \$476 billion in 2000, a figure that accounts for roughly one-tenth of global total tourism revenue, suggesting that, with domestic revenue, current total tourism revenue could be as high as five trillion dollars (Pizam and Yoel, 1996). The terrorism impact on the global economy is enormous. It leads to unemployment, homelessness, deflation, crime and other economic and social ills (Essner, 2003). The terrorism impacts the world economy to a larger extent. According to the report of World tourism forum's on the tourism economic impact (2011), tourism's expected total contribution for year 2011 is 13.87% towards world's GDP with increase of 4.5% than 2010 and it will create 258 jobs around the globe.

The tourism industry is one of the fastest growing sectors particularly in developing countries and has multidimensional effects. In the late 1960s and 1970s, the international tourism was prompted in the developing world in a way to reduce the government deficit and to increase the level of foreign exchange earnings. And in 1980s and 1990s, it was recognized that the tourism had a direct as well as indirect impact on the economic indicators such as government revenue, national income and employment. In addition, tourism is recognized as a means to diversify the economy and reduce reliance on traditional agriculture and industry (<http://www.erf.org.eg/html/btrade1.pdf>). Thus, the present paper evaluates the impact of tourism in the developing country like India.

The tourism sector contributes a lot towards the economic development but the terrorist activities cost a lot in the destruction of this economic development to the target countries. For example, the bombing of the U.S. embassy in Nairobi in 1998 and of a beach hotel in Mombasa in 2002, as well as an unsuccessful missile strike against an airplane chartered by Israeli tourists, have forced governments around the world to warn their citizens that Kenya is unsafe for tourist travel. This has cost Kenya

at least one million dollars per day. After the September 11, 2001 attacks, the U.S. government expenses on anti-terrorist activity increased by 20 billion dollars. After the 26/11 attack, the Government of India has admitted that the number of tourist arrivals in India had dropped by 3.3% due to terrorism but also added that the reasons apart from terrorism were global meltdown and swine flu scare. The figure of foreign tourists' arrivals had crept down to 5.11 Million foreign tourists in 2009 from 5.28 Million in 2008. Thus the objective of the present paper is to evaluate the impact of terrorism on the financial performance of tourism industry.

The paper is divided into eight sections. The next section reviews the relevant existing literature on terrorism and its impact on tourism. Section III mention hypothesis. Section IV discusses the research design and methodology, and Section V presents the analysis of data. Section VI gives the discussion of findings and Section VII provides the limitations, Section VIII provides practical implications and Section IX gives conclusions and recommendations.

II. Review of Literature

Many studies have been spurred on terrorism and its impact on tourism. In late 2001, the International Labour Office in Geneva released a study about the social impact of events subsequent to September 11, 2001 on the hotel and tourism sector. Starkov (2001) have studied the impact of terrorism on travel and hospitality industry and found that there is a long lasting negative impact Makinen (2002) have studied about the effects of on the U.S. economy. The airline, tourism, and insurance industries are the sectors of the economy that are suffering the most harm from the terrorist attack. Bennett and Bray studied the global effects of September 11 attacks on tourism. The study argued that it is unreasonable that the international tourist would stop flying after the terrorists attacks. This is because in the modern era people need to fly to reach different destinations. Ahmed, Nawaz, Qazi, (2011) studied the impact of terrorism on tourism industry in Pakistan. The paper found that the terrorism has tremendously shattered tourism industry in the country.

Mitra (2005) found that increase in the incidence and destructive potential of terrorism can have disastrous economic consequences. It leads to the intensification of the climate of fear which paralyzes entrepreneurial activity, particularly business tourism. It has a negative effect on the demand for certain products, for instance, air

travel and hotel services. It has a destructive impact on the valuable capital assets and human resources, such as that affected by the September 11 attacks. A lot of government funds have to be diverted from directly productive uses to meet the need for increased security. The paper argued that the technological progress could be the one reason for the increase in terrorism.

Essner (2003) had studied the terrorist activity in Egypt. This study provides an insight into the impact of terrorist group named al-Gama'a al-Islamiya targeting international tourists in dozens of attacks, resulting in many fatalities and hundreds of casualties. The study found out that there is fall in the tourists due to the terrorism that has grown increasingly violent with time but curiously came to an abrupt end.

Poonam (2009) had argued that the stock market as it is driven by the investor's attitude, perception, and information, the unanticipated events like 9/11 impact the psychology of the investors and their consumption power. The paper had studied the impact of terrorists attack on the stock prices of the share of particular industry. The study found that the unanticipated events like Mumbai attacks alone could not influence the stock market. Gul, Hussain, Bangash and Khattak (2010) studied the impact of terrorist activities on the financial markets in Pakistan over the period of two years from 2006 to 2008. It found out that the extent and direction of relationship between the terrorist activities and three financial markets of Pakistan, which are the Karachi Stock Exchange, the FOREX market and the Interbank market. The paper found that the terrorist activities adversely affect the financial markets but the significance varies for different markets. Terrorist activities are not only responsible for the adverse performance; many other stochastic activities are also responsible for the adverse performance. Chesney, Reshetar and Karaman, Mustafa (2011) studied the impact of terrorism on the behavior of stock, bond and commodity markets. The paper compares the effect of terrorist attacks on financial markets with the impact of other extreme events such as financial crashes and natural catastrophes.

Abadie and Gardeazabal (2007) used a simple economic model to show that terrorism has a large impact on the allocation of productive capital across countries and reduces the expected return to investment. With this, the changes in the intensity of terrorism may cause large movements of capital across countries if the world economy is sufficiently open, so international investors

are able to diversify other types of country risks. Higher levels of terrorist risks are associated with lower levels of net foreign direct investment positions, even after controlling for other types of country risks.

The objective of the present paper is to take into account the role of terrorism on the tourism industry and to measure the impact of the terrorism on the financial performance of tourism industry.

III. Hypothesis

The purpose of this research design is to evaluate the following hypothesis:

H1. There is significant impact of terrorist attacks on the financial performance of tourism industry.

IV. Design/Methodology

Various studies have been done to measure the magnitude of the effect of an unanticipated event. The present paper studies the impact of an unanticipated event i.e., the 2008 Mumbai attacks (sometimes referred to as 26/11) on tourism industry. For measuring the impact on the tourism industry, the paper examines the effect of 26/11 on India Tourism Development

Corporation (ITDC), a public sector undertaking of the ministry of Tourism. The tourism industry in India saw a significant arrival of foreign tourists till November 2008. But the 26/11 attacks had completely changed the scenario and India figured out to be an unsafe country to visit. The main target of this terrorist group is tourists. Thus, this study examines the effect of this unanticipated event on the balance sheets of the India Tourism Development Corporation (ITDC). ITDC was incorporated on 1st October, 1966, and has played a key role in the development of tourism infrastructure in the country. It has been the prime mover in the progressive development, promotion and expansion of tourism in the country. To study the impact, the financial statements of ITDC from the financial year March 2006 to March 2010 is evaluated.

In order to obtain the objectives of this study, the financial performance of ITDC is evaluated. The key figures such as liquidity ratios, leverage ratios, per share ratios, profitability ratios, and direct foreign exchange earnings are evaluated. Liquidity ratios include the current ratio, the quick ratio and the inventory turnover ratio. Return on capital employed, return on net working capital and gross profit margin are evaluated for measuring the impact

on profitability. “Owners fund as % of total source” and “fixed assets turnover ratios” are taken for evaluating the leverage ratios and earnings per share; dividend per share and operating profit per share are taken as per share ratios.

and after the attack. The data source is journals, research papers, newspapers, periodicals, annual reports of ITDC etc.

The paired t-test is applied to check the impact on the financial performance of the tourism department before

V. Data and Analysis

Table 1 Leverage Ratios

	<i>Years</i>					<i>Per cent change</i>			
	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
Leverage ratios	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
Owners fund as % of total source	99.81	99.88	99.99	100	99.96	0.07	0.11	0.01	-0.04
Fixed assets turnover ratio	3.21	4.72	3.83	3.08	2.11	47.04	-18.85	-19.58	-31.49
Paired t-test for leverage ratios									
Degrees of freedom	calculated value				table value				
1	1.035503				12.706				

Table 2 Per share Ratios

<i>per share ratios</i>	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
EPS	6.8	6.4	6.2	3.6	0	-5.88	-3.12	-41.93	-100
Dividend per share	2	2	1				0	-50	
Operating profit per share (Rs)	4.69	6.18	6.65	-0.44	-4.26	31.76	7.60	-106.61	868.18
Paired t-test on Per Share ratios									
Degrees of freedom	calculated value			table value					
1	3.632696			12.706					

Table 3 Profitability Ratios

	<i>Years</i>					<i>Per cent change</i>			
	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
Profitability ratios	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
Gross profit margin (%)	8.06	7.08	9.23	-1.96	-14.96	-12.16	30.37	-121.24	663.26
ROCE (%)	32.4	35.7	26.8	12	-6.4	10.18	-24.93	-55.23	-153.33
RONW(%)	28.8	23.2	16.8	7.9	-4.5	-19.44	-27.58	-52.97	-156.96
Paired t-test for Profitability ratios									
Degrees of freedom	calculated value				table value				
2	15.79355				4.303				

Table 4 Liquidity Ratios

	Years					Per cent change			
	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
Liquidity ratios	2006	2007	2008	2009	2010	2006-07	2007-08	2008-09	2009-10
Current Ratio	1.57	1.4	1.71	2	1.68	-10.82	22.14	16.95	-16
Quick ratio	1.31	1.3	1.63	1.88	1.52	-0.76	25.38	15.33	-19.14
Inventory turnover ratio	91.87	310.99	208.59	49.54	31.37	238.51	-32.92	-76.25	-36.68
Paired t-test on liquidity ratios									
Degrees of freedom	calculated value		table value at 5 % significance level						
2	2.160227		4.303						

Table 5 Direct Foreign Exchange Earnings

	Years					Per cent change			
	2005	2006	2007	2008	2009	2005-06	2006-07	2007-08	2008-09
Direct foreign exchange earnings (Rs. in crore)	156.59	146.94	149.1	57.23	6.86	-6.16	1.46	-61.61	-88.01

VI. Findings

The financial evaluation of tourism industry, a case of ITDC for the given period shows the decrease in turnover and profitability during 2008-09. Table 3 shows that there is a significant difference between the calculated value and the table value. It suggests that the profitability of ITDC has decreased due to the terrorist attack.

Impact of terror attack is visible on the financial performance of the tourism industry. The decrease in the performance clearly indicates the impact of terrorism in the tourism sector.

The impact of terrorism on the leverage ratios is insignificant. It is evident from the present figures in the Table 1. As we can see that there is no huge change in the numbers of leverage ratios. Table 2 shows that the impact of terrorist attacks on the per share ratios of ITDC is insignificant. There is no significant change in the per share ratios of the ITDC before and after the 26/11 attack. Table 4 shows the negative trend in the liquidity ratios of ITDC after the 26/11 attack. This shows that the ability of ITDC to pay off its short-term debts obligations had reduced after the terrorists attack. The calculated value is less than the table value; it shows that there is significant impact of terrorist attack on the tourism department.

Table 5 shows that there is a drastic change in the direct foreign exchange earnings after the 26/11 attack. There is fall in foreign exchange earnings by 88.01 per cent.

The impact on the financial performance is mainly attributed to the terrorist attacks in Mumbai on November 26, 2008. It is due to the deteriorated confidence level of the tourists beyond the national boundaries. The profitability of the Corporation was also affected due to pay revision and global financial crisis.

VII. Limitations

This research attempts to examine the impact of terrorism on the financial performance of tourism industry. The findings of the study are developed upon analyzing the impact of 26/11 on the financial performance of ITDC, a public sector undertaking as a case study. This study, however, looks at terrorism and tourism in India only. As a result, there exist shortcomings that should be addressed in future and with more comprehensive study.

The study could be further extended to the other areas of finance too. For example, the impact could be studied on other industries as well. The further work could be done on other disciplines like studying the social and psychological impact of terrorist attacks on local people

and tourists.

Also, this study only examines the 26 November attack and does not account for other terrorists activities in India that might have influenced the financial performance of the tourism industry. The tourism industry in India is big on which the effect of terrorism may have a marginal impact.

VIII. Practical Implications

No one is sure for how long this slump in the Indian tourism industry will last. The findings of the study will have some useful managerial implications for the Ministry of Tourism. The Ministry of Tourism has the responsibility to formulate and implement policies and programmes for the development of tourism within the country and abroad by way of developing tourism infrastructure, publicity and promotion, dissemination of information, co-ordination and supervision of activities of various segments of industry such as hotels, travel agencies, tour operators, etc. However, the travelers confidence is one of the key factors that can keep the Indian tourism industry out of the recession.

IX. Recommendations and Conclusion

India's tourism economy is in decline in large part because of terrorism. The need of the hour is to fight against terrorism. It cannot be wiped out by few hands or by the use of force. It has to be combated by the combination of government machinery; in addition stringent laws, quick and firm system of justice that delivers harsh punishments to the victims. National strategy needs to be spelled out the threat and how it should be dealt at all levels.

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