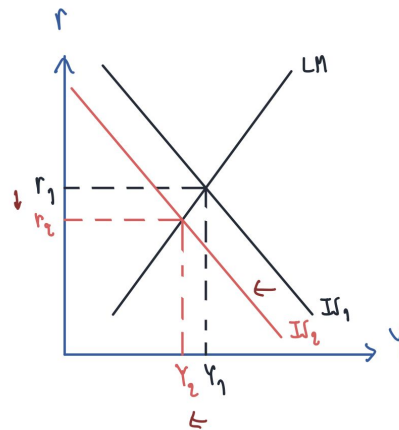


The 2001 Recession

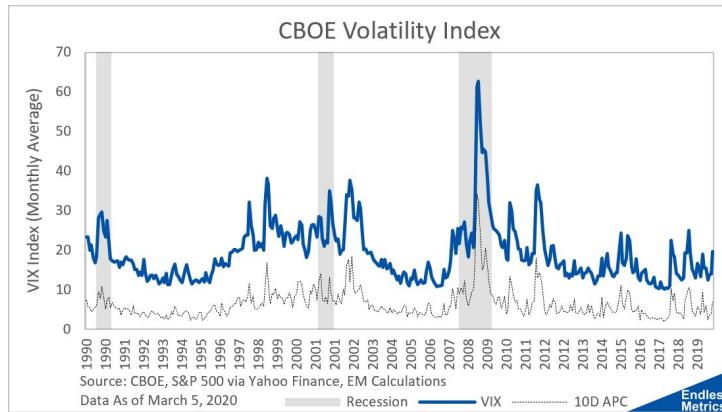
The 2001 recession was an eight-month economic downturn that began in March and lasted through November. More than 2.1 million people lost their job as the unemployment rate rose from 3.9% to 5.8%. GDP growth slowed to 0.8% compared to 3.9% which was the annual growth rate during 1994-2000. These took a couple of years before the recession ended.

Many people believe that the cause of the recession in 2001 was from the dot-com bubble. In the late 20th century, the internet created a positive attitude toward business and inspired many hopes for the future of online commerce. As a result, many internet companies were launched and the investors assumed that a company that operated online was going to be worth millions and give them a profit.

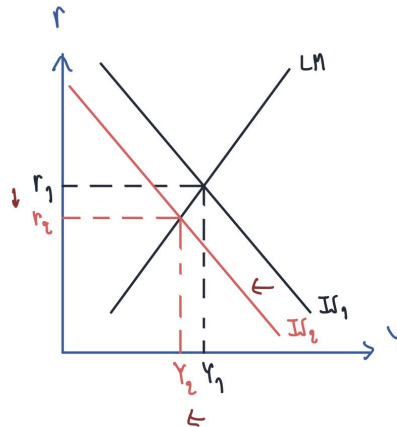
However, many dot-coms were not that successful and most that were successful were highly overvalued. In consequence, many of these companies crashed, leaving the investors with the significant losses. After the stock price drop, the investors basically lose the money at least one third of the original investment. These will generate a negative impact on the wealth of the investor which means the investors are less wealthy, so they need to reduce their consumption. Hence, aggregate expenditure (AE) will decrease and income (Y) also fall, resulting in an IS curve shift left.



Another strong belief of causing the 2001 recession is that 9/11. On the 11 of September 2001, 19 terrorists hijacked four planes in order to cripple the U.S. economy by destroying three centers of power: Wall Street, the Pentagon, and the White House. The planes crashed into 2 towers in New York city, the world trade center. The 9/11 attack worsened the downturn. The markets closed for several days after the attacks, and the New York Stock Exchange did not reopen until Sep. 17, 2001. That day, the Dow Jones Industrial Average (DJIA) had its largest one-day drop, falling 684.81 points or -7.1%.

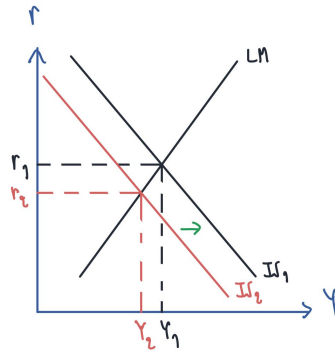


The volatility index is the way the measure the market risk, fear and stress before the investors take investment decisions. In the normal situation, volatility is moving very slowly but if it starts to move fast, something is going to happen. In 2001, the increase in volatility implies that people are so worried about the situation. With the worry, it increased in uncertainty among people which led to the lower investment as people are unsure of the situation. As a result, there is a fall in consumer and business confidence and then people will think to be more cautious on spending decisions. Of course, the consumers will lower their spending by reducing the consumption and investment. Thus, IS curve will be shifted left.



To end the recession, President George W. Bush began working with Congress to cut taxes immediately. The income tax relief to families retroactive to January of that year. EGTRRA lowered the maximum tax rate of 39.6% to 35%, the 36% rate to 33%, the 31% rate to 28%, the 28% rate to 25%, and some of the 15% tax rate to 10%. EGTRRA also expanded the Earned Income Tax Credit. It also doubled the standard deduction, raised the threshold for the 15% tax bracket for married couples, and doubled the child tax credit from \$500 to \$1,000.

These tax cuts by the Bush administration enabled taxpayers to keep more of their own money. The economy returned to growth in the fourth quarter of 2001. The Federal Reserve's expansionary monetary policy also contributed to the end of the recession. The Federal Reserve began lowering rates in January 2001, and continued to lower them by approximately one-half point each month, so that the rate was 1.82% (i.e., lower than 2%) by December 2001.¹⁵ This decision was made out of an effort to stimulate the economy by providing for more liquidity. These will cause IS curve shift back to the right from IS_2 to IS_1



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