

## California Earthquake Would Accelerate U.S. Mortgage Meltdown, Reveals Aon Benfield Study

by NAMIC

In light of current economic conditions, a major catastrophe such as an earthquake in California would bring new misery to both U.S. and international financiers, according to an analysis released Jan. 5 by Impact Forecasting LLC, a division of Aon Benfield, the world's premier reinsurance intermediary and capital advisor.

The "Annual Global Climate and Catastrophe Report: 2008" highlights that the lack of mandatory earthquake insurance in the state of California would result in high levels of mortgage defaults should an earthquake occur.

"Freddie Mac and Fannie Mae" the beleaguered financial entities that helped provide liquidity to the U.S. mortgage market "never required homeowners to purchase earthquake insurance for their properties," said Bryon Ehrhart, CEO of Aon Benfield's Analytics division. "Approximately 86 percent of Californian homeowners do not have earthquake coverage, despite most of them having mortgaged their homes. The 1994 Northridge Earthquake cost the mortgage industry up to \$400 million in mortgage defaults due to foreclosure expenses, property repair costs, lost interest income, write-downs of existing loan balances, and other administrative costs. It is hard to believe that there could be further downside for investors in mortgages than experienced in 2008 but the earthquake risk to the mortgage market is real."

The most significant natural catastrophe in 2008 was the tragic earthquake in China on May 12; very little insurance was in place on the destroyed properties, and the rebuilding costs are significant "currently estimated at \$146 billion. The largest insured loss event in 2008 was Hurricane Ike. Costs are still being tabulated, but it is likely to be the third most costly hurricane on record.

Additionally, the report reveals that between 1995 and 2008 there has been an increase in the average frequency of hurricanes in the Atlantic Basin. Average hurricane activity for the period stands at around eight hurricanes per year, compared to a 59-year average of 6.2 hurricanes per year.

Furthermore, hurricane intensity has risen dramatically in the same period with a 44.9 percent increase in Category 3, 4, and 5 hurricanes and a staggering 82.1 percent increase in Category 4 and 5 hurricanes.

Whether the increase in severe storms is a direct result of warmer Atlantic Ocean temperatures is still a hot topic of debate, according to Steven Drews, associate vice president and lead meteorologist of Impact Forecasting and co-author of the report.

"Debate on this subject will continue through 2009 as additional research by experts within the climatological and meteorological fields is peer reviewed, published, and debated on in various science and environmental publications as well at meteorological and climatological association events," he said. "As this debate continues and the insured risk along coastlines continues to grow, insurers and reinsurers need to become even more aware of their risk in hurricane-prone areas and continue to manage that risk through portfolio optimization and catastrophe modeling."

"The recent increase in hurricane frequency from 1995, at this time, cannot be attributed to one single event or factor," added Steve Bowen, meteorologist with Impact Forecasting and co-author of the report. "Scientists in our field continue to look for additional clues that might lead to conclusive evidence that this increase can either be explained by naturally occurring climatic cycles or anthropogenic global climate change."

Source: Aon Benfield

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