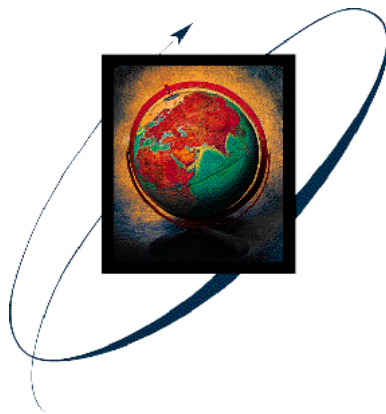


Sydney Hailstorm 14 April 1999: Impact on Insurance and Reinsurance

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Summary

During the early evening of 14 April 1999 a severe hailstorm swept north across the eastern edge of Sydney causing extensive damage to homes, businesses and vehicles. Hailstones up to 7 cm in diameter were reported. Current estimates (7 May 1999) by the Insurance Council of Australia - www.ica.com.au – put the insured losses at over one billion Australian dollars (US\$650 million). It is the most costly hailstorm in Australian insurance history, easily exceeding the March 1990 Sydney hailstorm which cost the insurance industry an estimated A\$385 million at current values. It is expected to become the largest insured loss from a single event in Australian insurance history, a record currently held by the December 1989 Newcastle Earthquake, for which the estimated insured loss in current values is A\$1.1 billion.

Damage

The hailstorm occurred within a thunderstorm which formed to the south of Sydney and affected almost the entire eastern seaboard suburbs of Sydney. An area of severe hail, which was the primary cause of damage, extended from the airport to the central business district as shown in Figure 1. Much of this hail was similar in size to tennis balls. One report suggested that the amount of hail which fell on Sydney during the storm was of the order of 500,000 tonnes. The thunderstorm was accompanied by strong winds and rain, the latter being a major cause of loss due to water damage to internal linings and contents.

The affected area has a relatively high concentration of values with a mixture of commercial and industrial facilities, including the airport, towards the inland side, and older, relatively affluent, medium density housing towards the seaward side. Houses in this area, most of which predate the 1930's with some being turn of the century and older, are predominantly roofed with terra cotta tiles, while many of the older industrial buildings have asbestos fibre cement roofs. Both of these materials are very brittle, and perform poorly under the impact of large hail. As a result most buildings in the severe hail affected area suffered significant roof damage, with consequent water damage to contents.

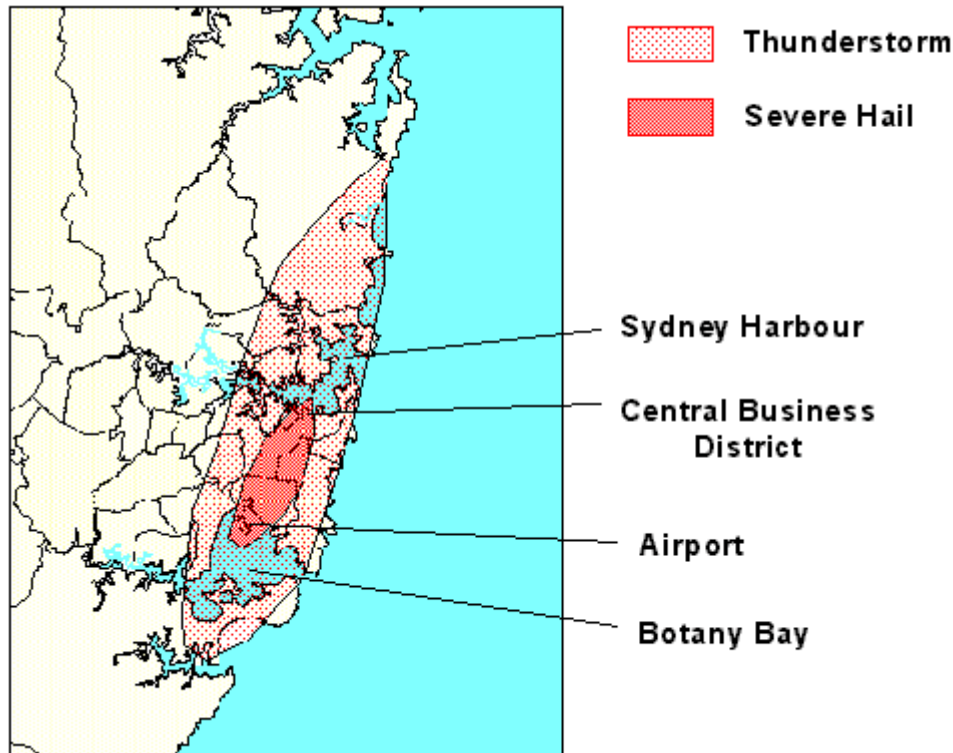


Figure 1 Map of Sydney showing storm affected area

Because of their older nature, many of the dwellings have limited or no space for garaging cars under cover, resulting in a high proportion of vehicles being parked on the streets. In the affluent suburb of Paddington many of these were relatively high value vehicles. Most of the uncovered vehicles in the severe hail affected area were damaged, with broken rear windows (toughened glass), cracked front windscreens (laminated glass), and denting of the metal bodywork.

Because of the large number of buildings affected, it took almost two weeks to temporarily cover all the buildings with tarpaulins. Losses due to water damage were exacerbated by periods of heavy rain and strong winds during this time.

In addition to building damage, approximately 30 planes at Sydney Airport were reported to have been damaged, resulting in significant disruptions to air travel around Australia the following day.

Insured Losses

At the time of writing (7 May 1999) claims reported to the Insurance Council of Australia total A\$940 million, and it is expected that the final cost to the insurance industry will be over a billion Australian dollars. Table 1 shows the make up of the reported claims to date.

Table1

Reported Claims to 7 May 1999*

*(Insurance Council of Australia Press Release 7.5.99)

Insurance Class	Number of Claims	Estimated Cost (A\$ million)
Home & Contents	32,000	310
Motor	43,000	300
Commercial	3,000	220
Aviation	NA	110

Table 2 shows the eight largest catastrophe losses in terms of current values experienced by the Australian insurance industry. It will be seen that it is likely to be over two and a half times as large as the previous largest loss from a hailstorm, and is likely to exceed the previous largest loss from any cause, which resulted from the 1989 Newcastle Earthquake. (In respect of the Cyclone Tracy losses it should be remembered that most of the homes and many of the other buildings were owned by the Federal Government, and uninsured.)

Table 2
Largest Australian Insured Catastrophic Losses 1967-1998*
**(Insurance Council of Australia)*

Event	Location	Date	Insured Loss (A\$ million)
Earthquake	Newcastle	1989	1125
Cyclone Tracy	Darwin	1975	835
Hailstorm	Sydney	1990	385
Cyclone Wanda	Brisbane	1974	330
Bushfires	Victoria/ South Australia	1983	325
Hailstorm	Brisbane	1985	300
Thunderstorm	Sydney	1991	225
Hailstorm	Sydney	1986	160
Hailstorm	NSW	1976	130
Cyclone Madge	Northern Australia	1973	150
Cyclone Althea	Townsville	1971	150

A factor affecting the repair costs will be a shortage of skilled building workers in the Sydney region due to a current boom in the construction industry buoyed by favourable economic conditions, the Sydney 2000 Olympics, and a rush to avoid the impact of a foreshadowed Goods and Services Tax (GST) on the cost of building. With the building industry already working to full capacity it has been suggested that commencement of repairs to many dwellings would be delayed by up to twelve months. As a consequence, the deployment of tarpaulins as a temporary measure is no longer considered a viable option. Tarpaulins are being replaced with sturdier materials as an interim measure, adding significantly to the cost.

The average assessed cost of repair of damaged homes appears to be about A\$10,000 and of vehicles about A\$5,000.

Impact of the Loss

A loss of a billion Australian dollars would represent roughly 15% of the Motor/Property premium pool (A\$6.56 billion) for the private sector in 1997 and less than 0.2% of Australia's GDP (A\$530 billion)*. This would make it a large loss, but not large enough to have a major financial impact on either the insurance industry or the national economy.

**(Australian Prudential Regulation Authority: Selected Statistics for the General Insurance Industry December 1997 – Latest Figures Available).*

By world standards a loss of a billion Australian dollars would be relatively small in that it would not feature in the Swiss Re list of the 40 most costly catastrophe insurance losses between 1970 – 1998. The smallest of these is the 1990 European winter storm Wiebke which in current values cost in the region of A\$1.5 billion.* It would have ranked fourth equal with the losses from tornadoes in the US at the end of June 1998 in the list of the most costly insured losses in 1998.

**(Swiss Re Sigma No.1/1999).*

Aon Re Australia has assessed the net cost to the Australian insurance industry of a loss of a billion Australian dollars to be in the region of A\$150 million to A\$180 million. A substantial proportion of this cost will be borne by four of the top ten insurers operating in the Australian Market. The balance of the billion dollars would be borne by the reinsurers, with an estimated 35% to 45% recoverable from overseas reinsurers.

General Economy

As a significant amount of the insured loss will be borne by overseas reinsurers, the hailstorm is expected to have a positive effect on the New South Wales economy. The most apparent winners are loss adjusters, building contractors and the motor industry. Suppliers of building materials, particularly roof tiles, will also benefit substantially from the loss.

Insurance Rates

The hailstorm is not expected to lead to an increase in insurance rates. Customers assume premiums are priced to cover natural hazards, irrespective of size. Across the board rate increases, immediately following a natural catastrophe, would therefore be unpalatable to the insurance client base, and would be a poor exercise in public relations.

Rate increases are already high on many insurer's agendas following poor underwriting results, low interest rates and the pending introduction of GST. IBNR (Incurred But Not Reported) claims will for example attract GST, while current premiums do not provide adequate revenues to offset this new impost. The introduction of GST will therefore have a far greater effect than the hailstorm on home and motor insurance rates.

Reinsurance Rates

There appears to be general consensus that the hailstorm will have little if any effect on worldwide reinsurance rates. While it will probably be Australia's largest insured loss to date, it is fairly low down on the worldwide loss log for catastrophes over the last forty years.

The hailstorm may have a localised effect of increasing Australian catastrophe rates for the lower layers. However Australian insurers have been at the forefront of purchasing long term catastrophe covers (LTA's) so there will be a limited number of catastrophe excess of loss covers renewed during the next 2 to 3 years (4 to 6 renewal seasons). While there may be limited layers, or tranches of limited layers due for renewal, we are unaware of any major "whole" programme due for renewal in 1999.

The current soft market spawned a significant amount of "opportunistic" underlying covers. It has been suggested that those purchased on an annual basis will not be renewed due to substantial rate increases for these layers following the hailstorm. Leaving aside these opportunistic buys, it therefore appears that the Australian insurance market will not immediately be subject to any significant increased reinsurance costs. There will, however, no doubt be some interesting discussions when the LTA's expire, particularly as a substantial number of these will expire when the full extent of the April 1999 Sydney Hailstorm is no longer a matter of speculation.

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