

Storm over Europe - An underestimated risk

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Zurich - Last December "Lothar" and "Martin" demonstrated to the insurance sector in Europe the enormous potential for catastrophe claims arising from winter storms. Although experience over the last fifty years shows that insured storm damage of the order of 7 billion US dollars can be expected every ten years in Europe, this risk is often underestimated. A new Swiss Re publication describes the phenomenon of European storms and the implications for the insurance industry.

"Lothar" and "Martin" caused economic losses of around 12 and 6 billion US dollars, respectively. Of this sum, 5.8 and 2.4 billion dollars, respectively, were insured, and 3.8 and 1.6 billion dollars, respectively, were covered by reinsurance policies. These sums are at the upper limit of losses caused to date by winter storms in Europe

Studies indicate that storm events involving damage in excess of one billion US dollars and a recurrence cycle of 2-3 years across the whole of Europe can be expected to occur more frequently than is generally assumed. Swiss Re expects incidents involving losses on the "Lothar" scale to occur every 8 - 10 years. Primary insurers and reinsurers who base their "risk management" exclusively on the most recent claims experience have significantly underestimated the storm risk. In fact, insured storm losses of the order of 30 billion US dollars are perfectly realistic for Europe and occur, on average, every 100 years.

An overoptimistic risk assessment leads to inadequate storm premiums which, in the longer term, are unable to cover the expected claims. The margin required by the reinsurer for the risk capital supplied can no longer be guaranteed.

Sound modelling of the storm risk is vital in assessing the effects of the latest storm incidents in Europe on the insurance sector and ensuring a pricing structure for (re)insurance that is matched to the risks involved. Swiss Re has therefore developed a probabilistic risk analysis model designed to perform such calculations.

How often do winter storms occur in Europe? And what potential losses are involved? What effect does global warming have on the formation of storms? And how should the insurance sector deal with this risk? The new Swiss Re publication not only poses these questions, but also provides the answers.

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