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MARKETS

Hurricane Harvey Unlikely to Damage Insurers' Balance Sheets

Personal and commercial insurers have record levels of capital with which to absorb potential losses

A store in Rockport, Texas, was damaged by Hurricane Harvey. **PHOTO:** MARK RALSTON/AGENCE FRANCE-PRESSE/GETTY IMAGES

By Nicole Friedman and Leslie Scism

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The insurance and reinsurance industry has a fatter-than-ever capital cushion to absorb losses from Hurricane Harvey, executives and analysts say.

The damage from the Category 4 storm, which hit the Texas coast on Friday, is far from being tallied. It is the first major hurricane to make landfall in the U.S. in more than a decade, and torrential rain will continue this week to cause widespread flooding.

Harvey's timing is good for insurers and insurance customers from one perspective: Personal and commercial insurers have record levels of capital, the money they have on hand that isn't required to back obligations. With insurers' overall strong capital position, Harvey is unlikely to cause extensive damage to the industry's financial strength, though it could hurt quarterly earnings for those carriers with blocks of business in hard-hit areas.

Most residential flooding isn't covered by private-sector insurers, but is the responsibility of the U.S. government's National Flood Insurance Program. Many carriers, however, do sell flood insurance to businesses.

Analysts estimate it would take $100 billion or more of losses in a 12-month period to cause distress within the insurance industry. Hurricane Katrina in 2005, the costliest hurricane in U.S. history, caused nearly $50 billion in insured losses in 2016 dollars, according to Wells Fargo Securities LLC.

"You would need to see a significant level of insured losses to have an impact on the excess capital of the industry [and] have a material impact on the pricing environment," said Elyse Greenspan, an analyst at Wells Fargo Securities last week.

Insurance company stocks didn't sell off Friday as they sometimes do during natural disasters. The property-and-casualty insurance subsector of the S&P 500 rose 0.6% Friday, compared with a 0.2% gain for the index overall.

Years of moderate damage from natural disasters have bolstered insurers' capital bases, as they have had to pay out less in claims. In addition, new capital has poured into the industry from pension funds, hedge funds and other investors seeking better returns as interest rates have globally remained low for nearly a decade.

U.S. property-and-casualty insurers had $709 billion in surplus in the first quarter of the year, a record high, according to trade group the Insurance Information Institute. That means the industry had $1 in surplus for every 75 cents of net premiums.

In Texas, home and car-insurance costs have been rising due to hailstorms and other factors. Harvey could lead to further price rises, said James Lynch, chief actuary at the insurance institute. But to cause nationwide price increases, "it would have to be something that spooked the market in a way that it hasn't been spooked by events like that in the past," he said.

While the industry is strong overall, there could be some hit to insurers with large Texas operations. Insurers are preparing for hundreds of thousands of claims from homeowners, car owners and businesses. The top homeowners' insurers in Texas are State Farm, Allstate Corp. and Farmers Insurance, according to ratings agency A.M. Best.

"At the end of the day, it's the individual insurers and their exposure in the region," said John Iten, a director with S&P Global Ratings.

Farmers projected Friday that half a million customers or more could be affected by the hurricane, said Jarrod Murrieta, the company's head of claims catastrophe response. Due to heavy rain and flooding, claims adjusters probably won't start assessing most of the damage until the middle of the week, he said.

Severe flooding can damage vehicles too. State Farm, Berkshire Hathaway Inc. 's Geico and Allstate are the top personal auto insurers in Texas.

The worst damage from the storm is expected to be caused by flooding, which largely isn't covered by homeowners' insurance. Home insurers protect against damage from wind, fire, hail and some other causes, but flood damage is typically borne by the National Flood Insurance Program. The U.S. program also sells coverage to small businesses and people who are renters.

Many private-sector insurers sell flood coverage to bigger businesses, and some, like American International Group Inc., have begun offering or are expanding coverage available to homeowners.

Hurricane Harvey could cause losses for holders of catastrophe bonds. So-called cat bonds are sold by insurers or by large entities seeking insurance, like transit agencies. Investors receive interest payments, but they lose their principal if certain disasters like hurricanes occur.

Catastrophe bond issuance hit a record high in the second quarter, according to reinsurance broker Aon Benfield. More than $26 billion of cat bonds were outstanding as of June 30. At the same time, economic losses from disaster events have totaled just $44 billion globally in the first half of 2017, compared with the 10-year average of $120 billion for that time period, reinsurer Swiss Re said in an estimate this month.

Even if Harvey leads to losses, appetite for cat bonds is expected to remain strong because they offer diversification to pension plans and other large investors.

"We don't see [Hurricane Harvey] as a disruptive type of event" in the cat-bond marketplace, said Paul Schultz, CEO of Aon Securities.

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