Ask Stan, the Insurance Man

Stan,

Why do house insurance rates/premiums increase after a major catastrophe like a hurricane?

Stormy

Dear Stormy: The simple answer is, to stay in business. Insurance companies have to increase premium rates to replenish their financial reserves after meeting multiple insured customers' claims following a major wide-spread catastrophe.

After all, they need to be able to provide enough premium income to keep their business going as well as to provide returns to shareholders who may have invested in the company. Insurance rates are very much controlled by what happens in the Reinsurance Market.

The Reinsurance Market is the place where Insurance Companies go for insurance, hence the name 'reinsurance.' It's a safety net of sorts. For instance, if need be after a major catastrophe such as a hurricane, the insurance companies can call on their reinsurance treaties to pay for the claims that surpass their deductible levels. If it is a very bad Category 2 or higher hurricane, the damages could be in the millions of dollars.

Reinsurers are in business to make a profit too, so they may increase the purchase cost to Insurers of further reinsurance. Insurers in turn, many times have no choice but to pass some of the rate increase on to policyholders.

Prices can also go up after a storm as the perception of the risk has changed, for example, the pricing in Cayman changed fundamentally after Ivan as Insurers & Reinsurers realized that they weren't adequately pricing in the cost of the flood/surge risk in their models.

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