

WEATHER PRODUCTS

Part Three: Hurricanes and Equities – Cross Market Opportunities

Hedging Hurricane-Sensitive Stock Exposure
with CME CHI Products

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Lessons from a Quiet Storm Season

By Eric Berger
Houston Chronicle
Nov. 29, 2009

Hurricane Season Ends with a Whimper

By Anthony R. Wood
Philadelphia Inquirer
Nov. 30, 2009

Shhhhh! 2009 Hurricane Season Ends with a Whisper in Southwest Florida

By Elysa Batista and Tara McLaughlin
Naplesnews.com
Nov. 29, 2009

Hurricane Season Ends on a Mild Note: Thanks to El Nino, Quietest Year Since 1997

By Ken Kaye
Orlando Sentinel
Nov. 30, 2009

Quiet 2009 Hurricane Season Comes to an End

By Mark Schleifstein
The Times-Picayune
Nov. 30, 2009

Atlantic Hurricane Season Has Fewest Named Storms in 12 Years

By Brian K. Sullivan
Bloomberg
Nov. 30, 2009

The 2009 hurricane season ended on November 30th. In the media, the common theme was that the entire event was virtually a dud.

Almost a year before these headlines hit the press, December 10, 2008, to be exact, CNN proclaimed: "Forecasters: 2009 to bring 'above average' hurricane season." The intention here is not to discredit the forecasters, but rather, to note the inaccuracy of predictions and forward looking statements and to make the point that the imprecision of storm predictions creates additional financial uncertainty.

With that in mind, the following is a forward look for the reader, a road map based on past events that might indicate where to look in the future. The premise of this series of articles has been that certain companies, industries and business sectors have intrinsic liabilities and benefits tied to hurricanes. These financial exposures to storms can be mitigated, to a certain extent, by hedging with CME Hurricane Index contracts (CHI).

Following are additional examples from recent years in which the dots have already been connected; the dots between shareholder value and the valuation of storm monetization embedded in the CHI contracts. A review of these selected pairings using anecdotal material coupled with the financial reports of dollar damages and theoretical CHI values may indicate areas where investors, hedgers, speculators, risk avoiders and opportunists might find monetary stability in synthesizing the pattern implied by the connected dots.

1999: FLOYD

PECO reported that Hurricane Floyd was the second worst storm in its history. Power outages lasted as long as 36 hours, impacting 400,000 of the utility's customers.

PECO, a utility company is now part of Exelon (NYSE:EXC)

Extensive flight disruptions hit Delta, Continental and AirTran airways.

Delta Airlines (NYSE:DAL)

Continental Airlines (NYSE:CAL)

AirTran Holdings (NYSE :AAI)

Waste Industries in Raleigh, N.C., lost 10 cents per share due to high winds and flooding that affected collection, transfer, disposal and recycling activities across the company's commercial, industrial and residential customer base.

Waste Industries Inc. (Nasdaq:WWIN)

2002: ISIDORE AND LILI

95 percent of crude oil and 60 percent of natural gas operations in the Gulf of Mexico were shut down between Sept. 25 and Sept. 30 due to Hurricanes Isadore and Lili. This disruption of domestic energy supply affected many companies, large and small. Nabors Offshore, servicing BP installations, suffered capsized vessels and ultimately evacuated all personnel. Rowan-Houston experienced a collision that led to the sinking of a rig. W-H Energy impacted equipment utilization in their Gulf operations.

Nabors Industries Ltd. (NYSE:NBR)

Rowan Companies Inc. (NYSE:RDC)

BP PLC (NYSE:BP)

W-H Energy Services Inc. (Nasdaq:WHES)

Pemco Aviation experienced a \$5 million revenue delay from deliveries moved forward by several months from these storms. The company provides aircraft modification services as well as cargo systems and rocket control systems to the U.S. Government.

Pemco Aviation Group (Nasdaq: PAGI)

2003: ISABEL

This storm slammed into the heart of Dominion Virginia Power's service territory. Unrelenting rain driven by 100 mph winds uprooted trees and brought down limbs causing outages for over one million Dominion customers in the state, and another million went without electricity in North Carolina. According to Thomas E. Capps, Dominion's chairman, president and CEO, "Hurricane Isabel was by far the worst natural disaster in our company's history." After massive disruptions to emergency repair and reconstruction procedures, the company literally rebuilt portions of its distribution system from scratch. The final loss in relative terms was "a 4 cent per share operating earnings impact from hurricane-related lost sales margin," according to the company.

Dominion Resources (NYSE:D)

2004: FRANCES, IVAN AND JEANNE

Hurricane Ivan was terrible, indeed, to Alcoa. Before plowing north to hit Alabama and Louisiana, Hurricane Ivan smashed into Jamaica, and damaged the company's bauxite mining and refining operations there, taking \$7 million out of Alcoa's bottom line. Once it pounded the Gulf Coast and headed inland, Ivan left a path of wind destruction, intense flooding and power outages. Hurricane Frances cracked her violent whip during the Labor Day weekend, and knocked a few cents off the earnings for Walt Disney, which had to close several of its theme parks. Office Depot of Delray Beach, Fla. lost sales from a four-day closure at its headquarters there. Hurricane Jeanne was quite deadly, causing about 2,800 deaths in and around the northern Haitian city of Gonaïves, which was practically washed away by mudslides and flooding. Federated Department Stores reported Jeanne was the culprit in a \$10 million shortfall at its Florida stores, a couple of cents lost for shareholders in the third quarter, but the four storm-related deaths in the state were a footnote, considering the gruesome havoc wreaked by Jeanne in Haiti.

Alcoa (NYSE:AA)

Disney (NYSE:DIS)

Office Depot (NYSE:ODP)

Federated Department Stores (NYSE:FD)

DATES FOR HURRICANES REFERENCED:

Year	Dates	Storm	Location(s)*	Category**	Deaths†	Damage	CHI‡
1999	Sep 7-16	Floyd	Bahamas North Carolina	4	57	\$4.5B	22.9/9.6
2002	Sep 14-27	Isidore	Cuba Yucatan Louisiana	3	4	\$970M	8.4/NA
2002	Sep 21-Oct 24	Lili	Caymans Cuba Louisiana	4	15	\$882M	12.3/5.2
2003	Sep 6-19	Isabel	North Carolina	5	16	\$3.6B	21.8/7.7
2004	Aug 27-Sep 8	Frances	Bahamas Florida	4	7	\$9.6B	15.2/6.6
2004	Sep 2-24	Ivan	Jamaica Caymans Cuba Alabama Louisiana	5	92	\$17.2B	23.5/13.5
2004	Sep 13-28	Jeanne	Guadeloupe Puerto Rico Dominican Rep. Haiti Bahamas Florida	3	3,035	\$7.0B	8.0/8.0
			*Landfall	**Saffir-Simpson Hurricane Scale	†Directly Caused		‡Maximum and Settlement

As we learned from Hurricane Katrina, the scope of a hurricane can transcend the dimensions of wind speed, storm radius and lost dollars. The death, suffering and devastation to our social, psychological and cultural fabric can't be healed, or hedged, with any index, no matter how well devised by its engineers.

In the final analysis, it is the insurance industry that provides much of the connective glue between storms and money. The bulk of the CHI transactions executed to date have all involved insurers or reinsurers. According to Brent Winans, VP of risk management services at Plastridge, an insurance agency in Delray Beach, "Even with no landfalls for four years, Florida's hurricane insurance market is a house of cards." Adds Winans, "If a worst-case storm hits us in 2010, billions of dollars in claims will go unpaid until the federal government bails us out or Florida is able to float the largest state bond issue in U.S. history. Those of us who understand this peril are hoping that CME's Hurricane Index options can provide savvy buyers with a powerful non-insurance tool to manage their hurricane risk." Mr. Winans is among those who see the capital markets as providers of incremental risk capacity beyond traditional insurance.

Mother Nature may be the perennial card dealer, but she also has the power to breathe with a mighty exhale and blow that house down. Without making one of those forward looking statements about the prospect of cascading piles of aces, deuces, jacks and queens, now, as 2010 is upon us, let's consider the prognostications already being made in the media.

Forecasters Predict 11 to 16 Storms Next Year

By Kate Spinner
Sarasota Herald-Tribune
Dec. 9, 2009

Hurricane Team: 2010 to be Above Average

By Eliot Kleinberg
The Palm Beach Post
Dec. 9, 2009

An Active 2010 Hurricane Season?

By David Tewes
Victoria Advocate
Dec. 9, 2009

2010 Hurricane Season Predictions Scatter All Over the Map

By Emily Nipps
St. Petersburg Times
Dec. 20, 2009

U.S. Hurricane Odds are Above Average in 2010

By Joseph B. Treaster
UPI.com
Dec. 30, 2010

These are the “paper positions.” The CME Hurricane Index contracts for 2010 are now available for trading by those risk holders, risk avoiders, traders, investors and speculators ready to take actual positions for the coming hurricane season.

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