

Bad Data

ACTUARIES HAVE A HARD TIME modeling for large-scale terrorist events. There just aren't enough of them. They can model for earthquakes and hurricanes because they've got plenty of data to work with. Not so for terrorism. There's 9/11, of course. And 3/11 and 7/7 and 7/21. Then there's Sharm el-Sheikh, and the Taba Hilton, and the Bali nightclub, and Beslan, and the U.S.S. Cole, and the Khobar Towers, and ...

Even so, actuaries say, it's the large-scale, World Trade Center-sized disasters that are (thankfully) scarce. One incident, no matter how traumatic, isn't enough to be able to predict the economic consequences of the next one.

Well, data are helpful, but be careful what you wish for.

Sometimes, actuaries and insurance people can sound calous when they talk about the cost of terrorist attacks in dollars and cents. After all, it's only stuff; it's the loss of life that really counts. Which is true. But while the bomb irrevocably destroys the lives of its victims, it's the economic devastation in the aftermath that keeps on destroying the lives of the survivors.

Make no mistake, economic devastation is what the terrorists are after, just as much as human devastation. According to figures compiled by the Organization for Economic Cooperation and Development, the attack on 9/11 cost \$28 billion in loss of physical assets and cleanup and \$32 billion in insured losses (business interruption, workers' comp, loss of life). It also added up to 3 percent of the cost of business transactions to cover the improved security measures. And that's probably not the half of it.

The stock market seems to have proved more resilient than expected. Though it took many months to recover from 9/11, there seems to be an expectation now that terrorism is a cost of doing business, to which world markets adjust accordingly. But Wall Street still isn't back to pre-9/11 levels.

Insurers can exclude terrorism, of course, which may save them from insuring bad risks. But it ends up bankrupting the

survivors. Or they can sell terrorism insurance for a price that's too easily affordable and end up bankrupting themselves. If they make it unaffordable, it's the same as excluding it anyway.

The government's response to the economic fallout of 9/11 was the Terrorism Risk Insurance Act (TRIA). The idea was to provide a backstop that would make terrorism insurance available and affordable in the United States, while allowing the insurance industry time to develop and improve mechanisms on its own. It was considered a temporary measure, set to expire at the end of this year. Now there are many in Congress and the administration ready to let that happen.

Insurance companies say they need more time to gather data and prepare for the inevitable. Meanwhile, they also have to prepare for the natural disasters that are just as inevitable, just as expensive, and certainly more frequent than terrorist attacks.

Those who are ready to pull the plug on TRIA are no better prognosticators than the actuaries who can't come up with solid numbers. They seem to be saying: "OK, it's been four years, nothing's happened, problem over. You guys are on your own."

Where on earth do they get that idea? European governments have been cushioning the economic shocks of terrorism with federal programs for years. Probably because they've had to deal with terrorism for years.

You wonder where those elusive weapons of mass destruction are? I'll tell you. They're in backpacks and parked cars and strapped around the waists of young fanatics. And they're not going away. Europe and Israel have learned the hard way not to let down their guard. Ever. I guess we'll have to learn that way, too.



EDITOR

Contingencies

Volume 17 / Number 5

PUBLISHED BY THE AMERICAN ACADEMY OF ACTUARIES

PRESIDENT
Robert E. Wilcox

EXECUTIVE DIRECTOR
Kevin Cronin

DIRECTOR OF COMMUNICATIONS
Noel Card

EDITOR AND ASSISTANT DIRECTOR FOR PUBLICATIONS
Steven Sullivan

PUBLICATIONS AND MARKETING PRODUCTION MANAGER
Joe Vallina

ADVERTISING
Mohanna & Associates

DEPARTMENT EDITORS
Thomas L. Bakos
Sam Gutterman
Yan Fridman
Richard T. Zatorski

PUBLICATION DESIGN & PRODUCTION
BonoTom Studio, Inc.

EDITORIAL ADVISORY BOARD
Julia T. Phillips, Chair
Dwight K. Bartlett III
Robert L. Brown
Frederick W. Kilbourne
Barbara J. Lautzenheiser
Bruce D. Schobel
Susan E. Witcraft

INTERNET ADDRESS
www.contingencies.org

Contingencies (ISSN 1048-9851) is published bimonthly by the American Academy of Actuaries, 1100 Seventeenth Street, NW, Seventh Floor, Washington, DC 20036. For subscription information and customer service, contact the *Contingencies* Subscription Department at the address above or (202) 223-8196. Advertising offices: Mohanna & Associates, Inc., (972) 596-8777, laurie@mohanna.com. Periodicals postage paid at Washington, DC, and at additional mailing offices. BPA circulation audited. (Basic annual subscription rate is included in dues. Nonmember rate is \$24.)

Copyright 2005. All rights reserved. This magazine may not be reproduced in whole or in part without written permission of the publisher. Opinions expressed in signed articles are those of the authors and do not necessarily reflect official policy of the American Academy of Actuaries.

Postmaster: Please send change-of-address notices for *Contingencies* to PMG Data, P.O. Box 7225, Bensenville, IL 60106-7225.

BPA
INTERNATIONAL

SOCIETY OF NATIONAL
SNAP
ASSOCIATION PUBLICATIONS