The Critical Need for Wind Pool Funding

Mississippi Economic Impact Study

Published February 17, 2009

More than three years after the worst natural disaster in United States history, the Mississippi Gulf Coast has seen its impressive recovery efforts compromised by a slowing national economy. High insurance rates have compounded this slowdown, and the private market shows no signs of returning in 2009. While long term solutions to lower the cost of insurance are being pursued, the likelihood of their implementation over the next three years is minimal. This paper explores a short term solution that will allow the Mississippi Gulf Coast to continue its recovery while long term plans are solidified, and it demonstrates how this short term solution will pay for itself.

Overview

More than three years and three full hurricane seasons have passed since Hurricane Katrina devastated the Mississippi Gulf Coast in 2005. Outside of the relative scare from Hurricane Gustav, which struck Louisiana and moderately impacted South Mississippi, the Mississippi Gulf Coast has experienced no major catastrophic events. Unfortunately, the private insurance market that left the Mississippi Gulf Coast in the wake of Katrina has yet to return and the following conditions exist:

- Tens of thousands of households are forced to rely on the wind pool for insurance, as the insurer of only resort.
- The immediate coastline remains largely in disrepair, with insurance either unattainable or unaffordable.
- Housing that would be considered affordable in other parts of the region are unaffordable because of the cost of high insurance, putting a strain on the working class that cannot be sustained in the long term.
- The overall recovery is threatened, as national publications such as Moody's Economy.com[1] have ranked the Gulfport Metropolitan Statistical Area last in the United States, or 382, in its vitality index, noting that if insurance rates are not reduced that reconstruction will not be completed and that pre-Katrina population levels will not return. Pascagoula's rating was 378.

While the prognosis above is dire, a short term solutions exists: if the wind pool is funded with a minimum of $20 million beginning in 2009 and lasting through 2011, then wind pool rates will be reduced which will afford long term solutions to be employed. **Subsidizing the wind pool is only a short term plan** that will stimulate the economy along the Mississippi Gulf Coast for two to three years while long term solutions are cultivated and the private market is given additional time to return. If this occurs the recovery efforts along the Mississippi Gulf Coast can progress more quickly and the Gulf Coast will continue to generate revenues that help drive the overall Mississippi economy.

A study commissioned by the Gulf Coast Business Council Research Foundation and conducted by the John C. Stennis Institute of Government at Mississippi State University demonstrates that in addition to aiding the completion of reconstruction this **$20 million in state funding will more than pay for itself** as a result of **NEW tax revenues to the state of Mississippi.**

Published findings from the Stennis Study

When researchers from the John C. Stennis Institute agreed to take on the task of determining any potential impacts of reducing wind pool rates in South Mississippi, they were asked to explore several avenues, to include the impacts of: sales of existing homes, new home construction, increases in discretionary spending, and rebuilding the immediate coastline. Results of the Stennis study demonstrate very clearly that the impact of selling 1,500 homes at an average price of $140,100, building 1,000 new homes, and passing 90% of the state appropriation of $20 million to wind pool policy holders will result in **NEW tax revenues to the state of Mississippi of more than $26.9 million** – and this does not account for the impact of rebuilding the immediate coastline. In other words, if the state incurs an expense of $20 million then the state might expect a return of $26.9 million, more than paying for the investment while also ensuring the full recovery one of its greatest revenue generators while other long term solutions are implemented.

Economic impact projections developed by researchers at the Stennis Institute are presented in the tables below. The State of Mississippi can expect to see income from sales tax dollars as well as income taxes, not to mention benefit from the overall economy on the Mississippi Gulf Coast receiving a tremendous boost. These projections assume that 90% of state appropriated wind pool dollars are passed along to wind pool policy holders and they are based on the first additional installment of $20 million. These projections are based upon an assessment that 1,500 homes valued at $140,100 are sold as a result of a $20 million stimulus. The fact that the total volume of residential homes sold in 2008 along the Mississippi Gulf Coast dropped by more than 40% from 2004 in 2008 and 19% from 2007 – this while the struggling national residential market only saw a 13% decrease in volume in 2008 from 2007 – reinforces this projection. Total homes sold in 2008 were less than 3,000 homes sold compared to pre-Katrina levels that were at 5,000 annually.[2] The negative correlation between the number of homes sold and wind pool policies in force is illustrated in the chart at the bottom of page 5 of this document.

Gulf Coast Projections

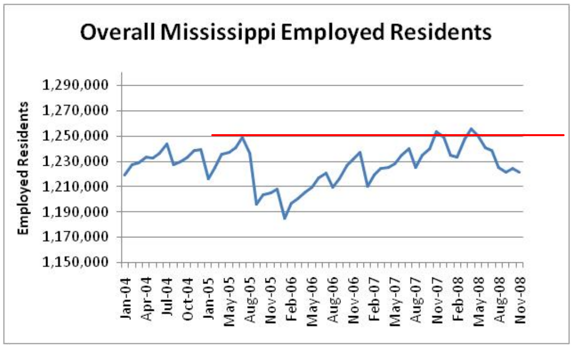
Sale of Existing homes						
			Income and Revenues per home	**Economic Impact from sale of 1500 existing homes**		**Taxes generated**
Real estate related activities			$ 12,609	$ 18,913,500		$ 945,675
Additional expenditures on consumer items			$ 5,171	$ 7,756,500		$ 542,955
Additional home construction			$ 17,513	$ 26,269,500		$ 1,576,170
				$ 52,939,500		$ 3,064,800
Multiplier Impact from sales of existing homes						
			Multipliers*		**Potential impact**	**Taxes generated**
Output multiplier			1.399	$ 52,939,500	$ 74,062,361	$ 5,184,365
Earnings multiplier			0.1612	$ 52,939,500	$ 8,533,847	$ 426,692
Job creation			13.5	$ 52,939,500	715	$ 1,020,050
						$ 6,631,108
Multiplier effect from reduction in insurance rates						
$ 20,000,000	$18,000,000	$ 72,000,000				$ 5,040,000
Impact of construction of 1000 new homes						$ 12,214,685
Total tax impact						**$ 26,950,593**

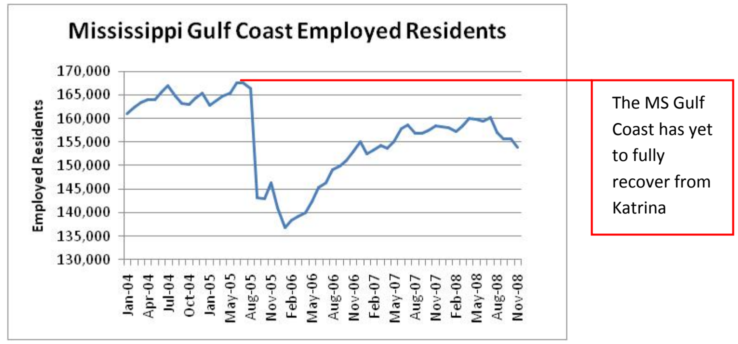
** Multipliers obtained from:*
"The Impact of Real Estate on the Florida Economy"
published by Shimberg Center for Affordable Housing
University of Florida

In addition to selling more homes, the Stennis Institute found that 715 jobs would be created for every $20 million injected into the wind pool, which would have an impact to the state general fund of more than $6.6 million dollars annually. Outside of real estate related activity, there would be a significant impact on discretionary incomes of the more than 40,000 wind pool policy holders along the Mississippi Gulf Coast. Conservatively, the Stennis Institute projected that these savings would be subject to an 80% propensity to spend, or a scenario where 20% of the rate reductions would be saved and that 80% of the rate reductions would be injected into the local and state economies. The end result would be an overall increase in consumer spending of $72 million for every $20 million that the state appropriates to the wind pool, which would have a direct impact on the state general fund of $5 million. Not included in the above projections is any impact on increased commercial activity along Beach Boulevard. In the recently published Fourth Quarter Regional Brief (Gulf Coast Business Council Research Foundation, February 2009) a survey of businesses located along Highway 90 before Katrina and in January 2009 found that only 20% of commercial businesses have returned to Gulfport and only 40% have returned to Biloxi. Undoubtedly, lowering insurance rates along Highway 90 would have a substantial impact on commercial activity along the coastline, generating millions of additional tax dollars for both local and state governments.

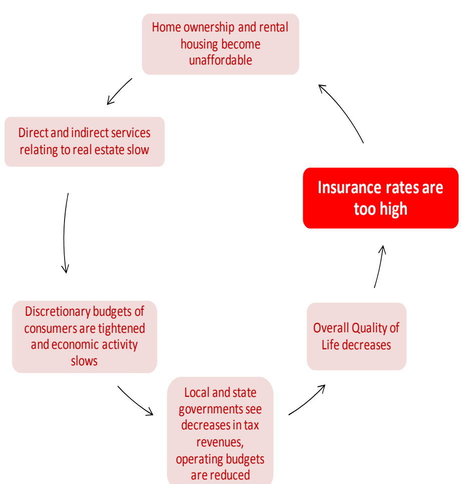
The negative impact of not funding the wind pool

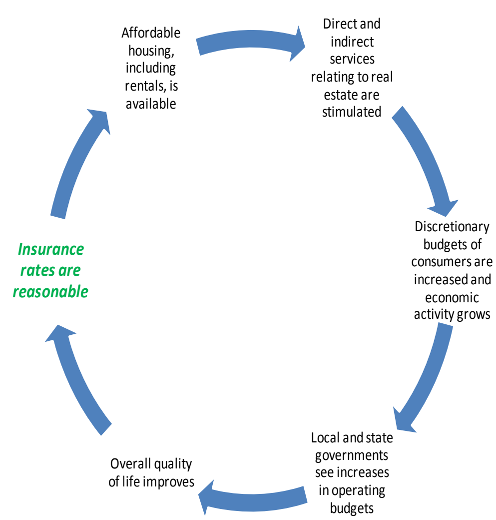
While there is strong evidence that funding the wind pool with an additional $20 million would pay for itself, the consequences of not funding the wind pool are potentially disastrous. While the entire state is suffering from the national economic recession, the Mississippi Gulf Coast is additionally challenged by insurance that is not affordable. Reference the two charts below that were obtained using data from the Mississippi Department of Employment Security.





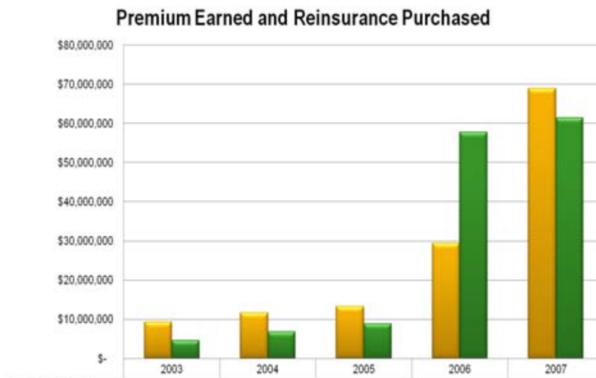
Not only has the number of employed residents along the Mississippi Gulf Coast yet to return, but exceedingly high insurance rates will ultimately result in existing residents of the Mississippi Gulf Coast relocating, in many cases out of state. If the Mississippi Gulf Coast does not complete its recovery in the next two years, there is a distinct possibility that any recovery efforts will take much longer, as an outward migration of residents will result in a vicious cycle of negative economic activity. For another perspective of how insurance is impacting the economy along the Mississippi Gulf Coast and ultimately the state, reference the exhibits below. The current cycle is depicted in the chart to the left. It is clear that the entire state of Mississippi is feeling some of the impacts, as both local and state budgets are underfunded in part because of the significant decrease in tax revenues that come from the Mississippi Gulf Coast. Reducing wind pool rates would help the Mississippi Gulf Coast to enter the cycle depicted to the right.





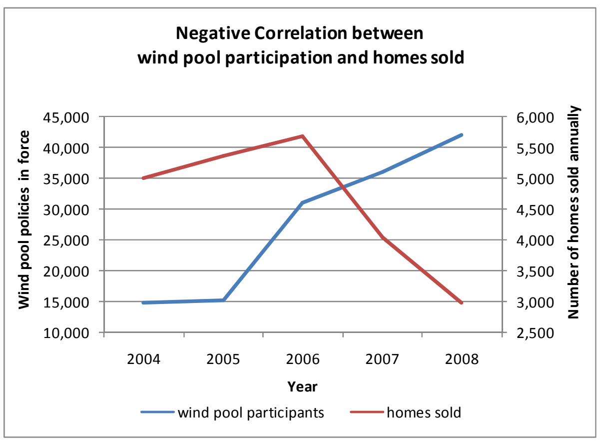
A brief history of the wind pool and its current status

In 1987 the Mississippi Legislature created the Mississippi Windstorm Underwriting Association (the "wind pool")[3]. The wind pool was designed to be an insurer of last resort and rates were scheduled intentionally higher than those of the private market. When Hurricane Katrina struck there were 16,000 policies in place. The impact of Katrina on the wind pool was substantial: after being faced with over $545 million in losses, the wind pool saw the reinsurance market tighten. For example, in 2006 the wind pool collected just under $30 million in premiums but it had to purchase over $57 million of reinsurance to operate that year. In 2007 premiums collected increased to over $68 million, which barely covered to cost of reinsurance. Evidence the chart to the right for a better understanding of how even after participation increased by over 230% the premiums collected were hardly adequate to purchase reinsurance.



	2003	2004	2005	2006	2007
Premium Earned	$9,268,971	$11,564,448	$13,282,881	$29,355,009	$68,855,666
Reinsurance Purchased	$4,594,708	$6,852,354	$8,817,760	$57,796,922	$61,429,793

Below is a graphic that demonstrates how increased participation in the wind pool has a negative correlation with the number of homes sold annually.



The number of wind pool policies in South Mississippi exceeds 42,000 as of late 2008 and continues to grow. This means that tens of thousands of households are required to pay thousands of dollars more for insurance annually, making housing unaffordable for most and suffocating the economy. These unaffordable rates have undoubtedly impacted the housing market, making it more difficult to sell homes because it is difficult, if not impossible, to find alternatives to the wind pool. The total home sales reported in MLS in 2008 were down by 2,000 from pre-Katrina levels, and the year over year decline was greater than the national average.

Source: Multiple Listing Services (MLS) and MWUA

Of concern to all Mississippi residents is State Farm's announcement in January 2009 that it would be dropping over 1.2 million policies over the next two years in Florida, likely forcing the majority of those policy holders into Florida's version of a wind pool[4]. While State Farm and other private insurers continue to assure business leaders and legislators that such a move is not on the horizon for Mississippi, it should be noted that similar promises were made in Florida in the past. This is not to criticize any decision that State Farm made in Florida recently, nor is it to diminish efforts underway on the private side of insurance in Mississippi; rather, it emphasizes the importance of addressing Mississippi's wind pool dilemma in 2009.

A viable solution has been offered

In 2007 the Mississippi Growth and Economic Development Act (HB 1500) was passed and authorized appropriating $20 million into the wind pool over a four year period. This resulted in a decrease in premiums in June 2008 of 7.7% for residential properties closest to the beach and up to 20% for properties furthest (commercial impacts were similar). While this appropriation produced significant results, average rates remain high along the Mississippi Gulf Coast, and significant opportunities for rate reductions exist. In the Stennis paper, the comparison is drawn between a household in South Mississippi compared to the rest of the state and it is demonstrated how households in the wind pool with gross annual income of $60,000 on average must spend $1,883 more annually for insurance. **Reference Appendix A for material that was presented in the recently published Stennis study.**

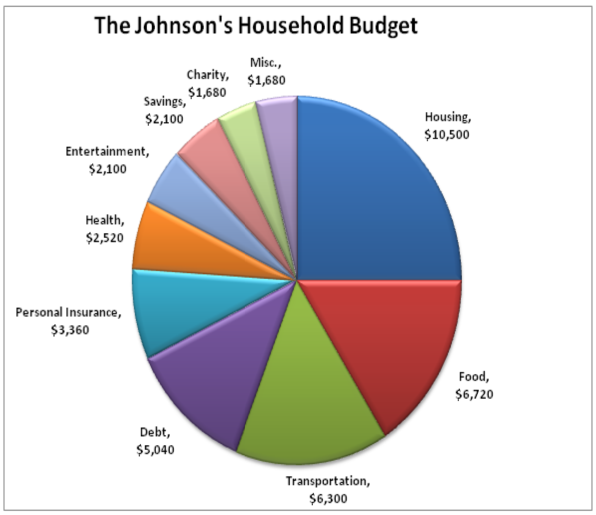
The proposed solution is straightforward: appropriate an additional $20 million into the wind pool and the affordability gap along the Mississippi Gulf Coast will be narrowed, resulting increased revenues to the general fund and allowing the Mississippi Gulf Coast to complete its recovery and continue to be a major economic driver for the entire state of Mississippi.

This summary paper reflects both the findings of the John C. Stennis Institute of Government at Mississippi State University and the Gulf Coast Business Council Research Foundation. When appropriate, information sources were cited. For questions about this paper, please contact the President of the Gulf Coast Business Council, Brian Sanderson, at (228) 897-2020. This paper is available for download in its entirety at www.msgcbc.org.

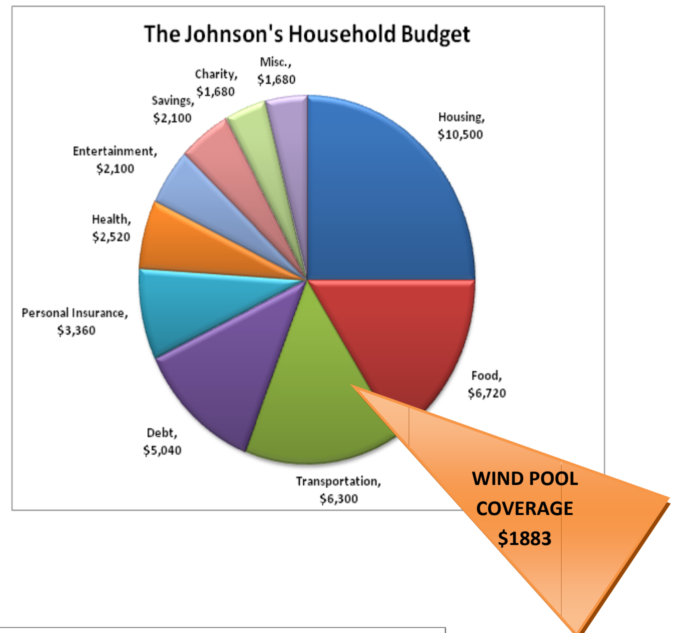
Appendix A – Typical Household Budget for combined gross income of $60,000 in North Mississippi compared to South Mississippi.

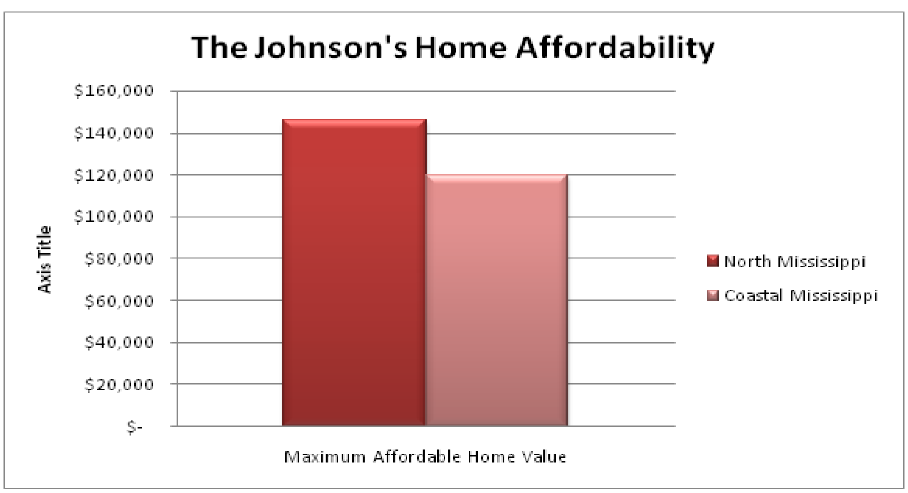
Source: John C. Stennis Institute of Government at Mississippi State University, 2009

North Mississippi



South Mississippi





[1] Moody's Economy.com November 2008
[2] Regional Brief – 4th Quarter 2008, The Gulf Coast Business Council Research Foundation
[3] Revamping the Wind Pool, Ron Peresich. *Mississippi Law Journal* Spring 2008 Vol. 77 Number 3
[4] TampaBay.com, January 28, 2009