

## News analysis

### Weather derivatives volume plummets

#### Notional values drop by 50+%, but there are some positives

The Weather Risk Management Association's (WRMA) annual derivatives market survey shows a more than 50% decline in notional values traded. WRMA observes that the drop in volumes mirrors the downturn in financial markets in general, but adds there were also several encouraging developments with non-US markets showing growth, while hedging activity associated with the renewables market is also on the rise.

The estimated notional value of weather derivatives – OTC and exchange-traded – traded in 2008/2009 was US\$15bn compared to US\$32bn the previous year, itself down from the all-time record year of 2005-2006 with US\$45bn. The total number of contracts traded during April 2008-March 2009 was 601,000 compared to 985,000 contracts in 2007-2008.

Temperature-related contracts remained the bulk of the trades. However, contracts for rain-related weather measures showed significant increases, as did activity in other highly structured products.

Although the overall number of contracts has decreased, WRMA notes that interest in weather risk management tools remained strong globally with weather contracts trading in North America, Asia, Europe and Australia.

In Asia, the number of weather contracts traded rose to 6,837 for the current year, compared to 1,940 in 2007-2008. In Europe, there were 34,068 contracts traded in 2008-2009 compared to the previous year's 25,290. The majority of the trades were on the Chicago Mercantile Exchange.

"The weather risk market continues to become more global," comments Martin Malinow, WRMA president and ceo of Galileo Weather. "WRMA is pleased to see increased interest for weather risk mitigation in Asia, Australia and Europe."

Not only is the weather market expanding geographically, but the scope of applications is broadening as well. "The rising use of renewable energy – solar, wind and hydro – will spur more interest in employing weather risk management tools," Malinow says. "Most renewable energy sources are tied to the weather and we're seeing increased interest from developers, operators and financiers in mitigating their weather exposure by using risk management tools."

The WRMA survey, which was conducted by PricewaterhouseCoopers (PwC), gathers data for the industry such as the notional value of the contracts, contract types and regional breakdowns. The survey runs from 1 April through to 31 March of the following year, in order to capture the complete winter and summer seasons.

WRMA engages PwC to conduct this annual survey to ensure that an independent third party collects and tabulates the data. As the weather market grows globally and in scope, the association says it will work to evolve the survey to better capture activity.

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