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Web site will let traders bet on hurricanes

BY MAYA BELL

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MIAMI - (KRT) - Storm watchers, listen up. If you think you have the weather knowledge and financial fortitude, you'll soon have the chance to bet for - or against - the coastline nearest you.

A trio of professors at the University of Miami is launching an electronic futures market to forecast where a hurricane will make landfall in the United States.

Traders who buy or sell the right spot at the right time can cash in, maybe clearing enough profit to buy a small generator.

Aptly called MAHEM, the Miami Hurricane Event Market isn't open for trading yet. Organizers are still refining the prospectus and plugging holes in their Web site, mahem.miami.edu, but MAHEM is slated to debut any day now - in the name of research and education.

"We are not gamblers. We are scientists," said David Kelly, an economics professor and one of MAHEM's co-founders, who acknowledges that some people will consider the market tasteless. "But if you go down that road, you could say buying stock in a pharmaceutical company is hoping people get cancer. I choose to look at this as a benefit to society by helping research on how to make a better forecast."

Anyone who opens a trading account can invest in MAHEM shares, which will consist of segments of U.S. coastline. But the hope is experts will make up the bulk of traders, bringing a knowledge of hurricanes and an incentive to grow their investment to the electronic trading pit.

Kelly and his collaborators define experts rather loosely - from actuaries in the reinsurance industry to Key West bar owners who have watched their share of tropical tempests. They will, however, recruit meteorologists.

"We're not trying to beat the National Hurricane Center at their game," said David Letson, another University of Miami professor who came up with the MAHEM idea. "There's no way we'll do that, but what we want to do is improve our understanding of how people use forecast information."

For now, MAHEM's principals, who also include University of Miami meteorologist Dave Nolan, are hoping at least 100 investors ante up. If so, here's how the market is designed to work:

Investors can open accounts by sending any amount from \$5 to \$500 to the Iowa Electronic Markets, or IEM, which is operated by the University of Iowa, a MAHEM partner. All IEM transactions are made electronically and posted in real time.

As soon as a tropical storm earns a name, the market will open, and online trading will begin. Depending where the storm is at the time, it will be declared an Atlantic or a Gulf storm, and only contracts, or shares, for that U.S. coastline will be sold.

Traders who buy their initial shares from the market itself will receive a portfolio of 10 contracts for \$1, which will be the highest value of winning contracts. Eight of the contracts will represent strike zones for eight different segments of either the Atlantic or Gulf coastlines, with each segment having roughly equal historical probabilities of landfall.

As the storm's path becomes clearer, trading should hit full swing, with investors setting the prices of individual segments based on where they think the storm is going. If for example, an Atlantic storm appears Miami-bound, investors will likely sell their North Carolina or New England shares for mere pennies.

Conversely, if they think there is less than a 50 percent chance the storm will blast Miami, they might sell their Miami area shares for 50 cents. If the storm indeed hits Miami, traders who previously bought Miami zone shares for 50 cents would double their money.

"With a maximum investment of \$500, nobody will get rich," said Forrest Nelson, an economist at the University of Iowa and one of the founding directors of the IEM. "But it might give someone some bragging rights."

There is, of course, the possibility a storm will strike elsewhere, never hit the United States or change coasts. That's where the remaining two contracts come into play. The ninth contract will represent a nonhit in the United States. The 10th will represent a storm that switches coasts, for instance following a path similar to that of Hurricane Emily.

Had MAHEM been open for Emily, investors who held on to that 10th contract would have received a new portfolio when Emily crossed an imaginary line separating Atlantic storms from Gulf storms, Letson said. Again, the portfolio would be worth \$1.

An economist at the University of Miami's Rosenstiel School of Marine and Atmospheric Science on Key Biscayne, Letson came up with the idea for MAHEM during last year's hurricane season, which brought an unprecedented four hurricanes to Florida.

A father of two young children, he also lives on Key Biscayne, a barrier island east of Miami and, like a lot of Floridians, spent almost half the year nervously watching, waiting and wondering whether he should evacuate his family.

But as an economist, Letson is also a fan of the Iowa market. Founded in 1988 by Nelson and two other professors at the University of Iowa's business school, the IEM pioneered the use of futures markets to forecast the outcome of events, most notably presidential and other elections.

More recently, the IEM created a closed market for health-care professionals to forecast hot spots for the flu. Eventually, directors hope to create one that will predict the next strain of flu.

"They're famous in the economics profession. We use them in the classroom and read papers by these guys," Letson said.

Which left Letson to wonder, "Gee, could we learn anything about hurricanes by setting up a market to forecast landfall?"

Nelson said he was immediately intrigued by the idea, which he called "fantastic." But not everybody agrees. State meteorologist Ben Nelson - no relation - said he worries MAHEM could generate conflicting messages when a hurricane threatens.

"We're a free-enterprise society, but we have to have one message, and that message is best relayed by the National Hurricane Center," Ben Nelson said.

Center director Max Mayfield was likewise puzzled how MAHEM could improve the center's forecasts. He was, however, sure of one thing: Neither he nor any other government meteorologist could invest.

"National Weather Services employees are not allowed to use their positions for personal gain, period. That means they couldn't participate," he said.

Which leaves two big questions: Who will, and how much will they know?

"At this stage, this is an experiment," the IEM's Forrest Nelson said. "It could be a total flop. Markets aren't magic. They're just as good as the traders and the information they hold."

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