Catastrophe Bonds

Source: BS

Catastrophe bonds, which have delivered substantial returns for investors, are now under scrutiny due to concerns that their risk-reward dynamics might unfairly disadvantage issuers, particularly in the Caribbean.

- Catastrophe bonds or **CAT bonds** are financial instruments that p**ay high returns to investors** in **exchange for bearing the risk of significant disasters.** These bonds are typically issued by insurers, or governments to obtain additional coverage for catastrophic events like **hurricanes, earthquakes,** or **floods.**
  - Catastrophe bonds allow **investors to receive periodic interest payments,** but if a predefined catastrophic event occurs, the **bond's principal is used to cover the issuer's losses.**
  - Payout conditions are **based on triggers** defined in the bond contract, which can be **parametric** (e.g. wind speed, seismic activity) or **indemnity (**e.g. actual loss figures reported by insurers).
- Recently, in Jamaica Catastrophe bonds have delivered double-digit returns, averaging around 15%, while **issuers face significantly increased costs**.
  - The bond issued by Jamaica was **not triggered despite the island being declared a disaster area** after **Hurricane Beryl**, raising questions about the bond's terms.
- Caribbean heads of government are seeking an examination of catastrophe bonds and insurance-linked securities to assess their fairness and market selection.

Read more: Catastrophe Bonds