Freddie Mac April 2016 Insight

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Life's a Beach

MCLEAN, VA--(Marketwired - Apr 26, 2016) - Freddie Mac (OTCQB: FMCC) released today its monthly Insight for April with a focus on the flood challenges the industry faces, the current system in the United States for dealing with flood risk, and some questions that will have to be addressed if climate change raises sea levels significantly.

Insight Highlights

- Insurance is an essential component of real estate transactions, and flood insurance currently makes it possible to obtain loans for homes in areas of identified flood risk.
- Some of the varied impacts of climate change -- rising sea levels, changing rainfall and flooding patterns, increasing temperatures -- may not be insurable. As a result, some important features of housing finance may have to change.
- A large share of homeowners' wealth is locked up in their equity in their homes. If those homes become uninsurable and unmarketable, the values of the homes will plummet, perhaps to zero. Unlike recent experience, homeowners will have no expectation that the values of their homes will ever recover
- In the housing crisis, a significant share of borrowers continued to make their mortgage payments even though the values of their homes were less than the balances of their mortgages. It is less likely that borrowers will continue to make mortgage payments if their homes are literally underwater. As a result, lenders, servicers and mortgage insurers are likely to suffer large losses.

Quote: Attributed to Sean Becketti, Chief Economist, Freddie Mac.
"One challenge for housing economists is predicting the time path of house prices in areas likely to be impacted by climate change. Consider an expensive beachfront house that is highly likely to be submerged eventually, although 'eventually' is difficult to pin down and may be a long way off. Will the value of the house decline gradually as the expected life of the house becomes shorter? Or, alternatively, will the value of the house -- and all the houses around it -- plunge the first time a lender refuses to make a mortgage on a nearby house or an insurer refuses to issue a homeowner's policy? Or will the trigger be one or two homeowners who decide to sell defensively?"

"Currently, under federal law, flood insurance is mandatory for all federal or federally-related financial assistance for the acquisition and/or construction of buildings in Special Flood Hazard Areas (SFHAs). In addition, Freddie Mac requires flood insurance before it will purchase a loan for a property in an SFHA. As the market shakes out in the affected areas some residents will cash out early and suffer minimal losses. Others will not be so lucky. And newcomers may appear, finally able to live out their dreams of living at the seashore, if only for a short time."

Freddie Mac was established by Congress in 1970 to provide liquidity, stability and affordability to the nation's residential mortgage markets. Freddie Mac supports communities across the nation by providing mortgage capital to lenders. Today Freddie Mac is making home possible for one in four home borrowers and is the largest source of financing for multifamily housing. Additional information is available at FreddieMac.com, Twitter @FreddieMac and Freddie Mac's blog FreddieMac.com/blog.