Severe Weather Patterns And Banking

lending risk management

Summary: Whatever your thoughts on climate change, severe weather patterns are affecting the real estate market. We provide you with an update.

Science and weather can be interesting. For instance, did you know that mild weather in the fall can mean we see bigger spiders inside our houses? Or that the chilliest temperature recorded was -89.2 degrees Celsius (-128.56 degrees Fahrenheit)? Or even that raindrops can fall at more than 30km/hr?

While you ponder these facts, we wanted to touch on the topic of severe weather and real estate today. Whatever your thoughts on climate change, severe weather patterns are affecting the real estate market. Flood prone communities are at risk of losing property value, and down the road, mortgage lenders could be affected. Because of this, various research has been conducted by 38 university professors and financial professionals and published by the Federal Reserve Bank of San Francisco.

As the director of the San Francisco Fed's Center for Community Development Investments notes, "The associated risks and effects of climate change are relevant considerations for the Federal Reserve." New risks are always important to assess for the financial industry, but how to manage these risks can be challenging.

The Fed is not advocating any new policy, but wants to help provide information and start discussions around the effects of climate change on the industry. The published research urges businesses and communities to work together to help manage these severe weather conditions, specifically in low or moderate income (LMI) areas that are most vulnerable. One economist at a western university finds that those properties most plausibly under water with one foot rise in sea level are already priced 15% lower than similar properties outside of the flood zone. These communities will need even more support, if these conditions worsen.

This situation is still developing, but some big banks are starting to take steps to incorporate this new risk. Take JP Morgan Chase and Wells Fargo--they put a price on mortgages for flood risk. They have decided to securitize some of these loans so as to spread the risks. For instance, they resell to Fannie Mae and Freddie Mac, which don't factor in climate change, when calculating the true value of mortgages.

For community financial institutions, it is not clear what steps to take yet. However, it would be prudent to stay aware of any consistent weather changes affecting your business customers. This should be included, of course, in your ongoing risk analyses. Also, keep talking to customers about what they are doing themselves to insure against additional weather risk. This is likely more natural for you, as you are more connected to your customers and your community. But, as you expand, this will become more challenging. So, make sure you keep this on your radar, and you will be more prepared, whatever the new weather patterns bring.

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