Flood risk has historically resulted in poorer performance for both individual mortgages and mortgage-backed securities.

The distribution of risks for residential real estate, including flood risk, depends largely on how these risks are allocated across individual mortgages and within mortgage-backed securities (MBS). This paper is the first to document how flood risks relate not only to individual mortgage performance and underwriting, but also how flood risks correlate to MBS performance and structure. Across residential mortgages we find that defaults are concentrated among the most flood-prone properties and this risk is somewhat offset by larger down payments and slightly higher mortgage rates. Even when mortgages are combined into MBS's, we show that average mortgage default within MBS's increases with average flood risk and that higher flood risk is primarily offset by increased credit protection or subordination; a one unit increase in flood risk is associated with a 2.6 percent increase in subordination. Ultimately, our analysis suggests that flood risk is reflected in mortgage-level performance and pricing and is partially, but not fully, accounted for in MBS deal-level performance and structure.

JEL classifications: Q54, R3, D89, G12

Article Citations


Related Research


Authors

Jacob Dice
Software Engineer

Jacob Dice is a Software Engineer in the Research Facilitation group at the Federal Reserve Bank of Kansas City. He holds a M.S. in Computer Science from the Georgia Institute of Technology and a B.A. in Economics and Physics from William Jewell College. As a research facilitator, Jacob partners with economists to accelerate policy and research code to efficiently scale across the Bank’s high performance computing (HPC) environment.

David Rodziewicz
Regional Research Senior Economics Specialist

David Rodziewicz is a senior economics specialist at the Denver Branch of the Federal Reserve Bank of Kansas City. His research focuses on energy economics, natural resource economics, climate change, and regional economics. His outreach efforts focus on the Rocky Mountain West region (Colorado, Wyoming, and northern New Mexico). Rodziewicz is also responsible for briefing the Kansas City Fed’s president – a member of the Federal Open Market Committee – on regional economic conditions as well as energy related issues. Prior to joining the Economic Research Department at the Bank in 2017, Rodziewicz was as an officer in the National Oceanic and Atmospheric Administration’s Commissioned Officer Corps, where he served as a deck watch officer in Alaska and database manager in Boulder. Earlier in his career, he worked in the financial services industry as a stock analyst, covering real estate investment trusts (REITs). Rodziewicz holds a master’s degree in Mineral and Energy Economics from Colorado School of Mines and a bachelor’s degree in Finance and Economics from University of Illinois.