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Perils of Climate Change Could Swamp Coastal Real Estate

Homeowners are slowly growing wary of buying property in the areas most at risk, setting up a potential economic time bomb in an industry that is struggling to adapt.

By IAN URBINA NOV. 24, 2016

MIAMI — Real estate agents looking to sell coastal properties usually focus on one thing: how close the home is to the water's edge. But buyers are increasingly asking instead how far back it is from the waterline. How many feet above sea level? Is it fortified against storm surges? Does it have emergency power and sump pumps?

Rising sea levels are changing the way people think about waterfront real estate. Though demand remains strong and developers continue to build near the water in many coastal cities, homeowners across the nation are slowly growing wary of buying property in areas most vulnerable to the effects of climate change.

A warming planet has already forced a number of industries — coal, oil, agriculture and utilities among them — to account for potential future costs of a changed climate. The real estate industry, particularly along the vulnerable coastlines, is slowly awakening to the need to factor in the risks of catastrophic damage from climate change, including that wrought by rising seas and storm-driven flooding.

But many economists say that this reckoning needs to happen much faster and that home buyers urgently need to be better informed. Some analysts say the economic impact of a collapse in the waterfront property market could surpass that of the bursting dot-com and real estate bubbles of 2000 and 2008.

The fallout would be felt by property owners, developers, real estate lenders and the financial institutions that bundle and resell mortgages.

Over the past five years, home sales in flood-prone areas grew about 25 percent less quickly than in counties that do not typically flood, according to county-by-county data from Attom Data Solutions, the parent company of RealtyTrac. Many coastal residents are rethinking their investments and heading for safer ground.

“I don’t see how this town is going to defeat the water,” said Brent Dixon, a resident of Miami Beach who plans to move north and away from the coast in anticipation of worsening king tides, the highest predicted tide of the year. “The water always wins.”

These concerns have taken on a new urgency since the presidential election of Donald J. Trump, who has long been a skeptic of global warming, claiming in 2012 that it was a concept “created by and for the Chinese in order to make U.S. manufacturing noncompetitive.”

A real estate developer, Mr. Trump is also the owner of several South Florida properties, including Mar-a-Lago, a 20-acre site that stretches between the Atlantic Ocean and the Intracoastal Waterway in Palm Beach.

Mr. Trump’s recent selection of Myron Ebell to lead his Environmental Protection Agency transition team intensified these worries in Florida and among many climate scientists. Mr. Ebell has helped lead the charge against the scientific consensus that global warming exists and is caused by people.

State lawmakers in Massachusetts and New Jersey are pushing to impose new rules on real estate agents and others, obligating them to disclose climate-related damage like previous flooding.

Banks and insurers need to protect their collateral and investors more by improving their methods for estimating climate-change risks and creating more standardized rules for reporting them publicly, economists warn.

In April, Sean Becketti, the chief economist for Freddie Mac, the government-backed mortgage giant, issued a dire prediction. It is only a matter of time, he wrote, before sea level rise and storm surges become so unbearable along the coast that people will leave, ditching their mortgages and potentially triggering another housing meltdown — except this time, it would be unlikely that these housing prices would ever recover.

"Some residents will cash out early and suffer minimal losses," he wrote. "Others will not be so lucky."

Bull's-Eye for Property Damage

Much of the uncertainty surrounding climate change focuses on the pace of the rise in sea levels. But some argue that this misses the point because property values will probably go under water long before the properties themselves do.

What is often called "nuisance" flooding — inundation caused more by tides than weather — is already affecting property values. Often just a foot or two deep, this type of flooding can stop traffic, swamp basements, damage cars and contaminate groundwater.

Florida has six of the 10 American urban centers most vulnerable to storm surge, according to a 2016 report from CoreLogic, a real estate data firm. Southeast Florida experiences about 10 tidal floods per year now. That number is likely to be around 240 floods per year by 2045, according to climate researchers.

In the past year, home sales have increased 2.6 percent nationally, but have dropped about 7.6 percent in high-risk flood zones in Miami-Dade County, according to housing data. Many coastal cities are taking steps toward mitigation, digging runoff tunnels, elevating roads and building detention ponds.

James Murley, Miami-Dade's chief resilience officer, said it was important to avoid spooking the market since real estate investment produces much of the revenue that pays for these upgrades. This balancing act is especially important in Florida because the state and localities rely heavily on property and sales taxes for funding such projects.

Florida is not alone. Forty percent of Americans live and work in coastal areas, and those who can afford it are protecting their investments by building private bulkheads and lifting their homes onto stilts. But skeptics question the logic of upgrading individual properties if the surrounding areas do not keep pace and flooding or the rise in sea levels swamps nearby roads.

For many home buyers and owners, the cost of flood insurance is a growing worry. As premiums rise, property values fall, a trend already hurting home prices in places like Atlantic City, Norfolk, Va., and St. Petersburg, Fla., according to local real estate agents.

Roy and Carol Baker, who now live in Sarasota, Fla., recalled trying for several months to sell their home in nearby Siesta Key in 2014. Interested buyers kept backing out of the purchase when they found out that the annual flood insurance premium was roughly $7,000, they said.

This experience will become more common, economists say, as the federal government shifts away from subsidizing flood insurance rates to get premiums closer to reflecting the true market cost of the risk.

As difficult as it is to predict the pace of climate change, modeling how it will affect the real estate market is even more complicated. Like a game of hot potato, builders, homeowners, banks, flood insurers and buyers of securitized mortgages try to hand off risky properties before getting burned. Developers erect houses and sell them typically within a couple of years, long before their investments depreciate. Banks earn commissions even on risky home loans before bundling these mortgages into securities and selling them to large pension funds, insurers or other buyers.

Home buyers tend to think short term, focus on what they can afford and hope that the local infrastructure keeps pace with the rise in sea levels. Home buyers are also generally on their own as they look at prospective properties and try to size up their risk, as real estate agents vary in what they disclose.

Most real estate agents say they try to tackle the issue head-on, providing clients with maps indicating federally declared high-risk flood zones, and using climate-change preparedness as a selling point, emphasizing if the house has a backup generator or shingles that can withstand hurricane-strength winds.

But real estate agents risk putting themselves at a competitive disadvantage by overstating threats. Good information is hard to come by. No one knows whether, when or by how much properties will depreciate, seas will encroach or flood insurance policies will change.

Valerie Amor, a real estate agent in Fort Lauderdale, said that, unlike most in her industry, she does a feasibility study before she assists in either buying or selling property.

"It should not be left as a moral or personal decision," said Ms. Amor, adding that more disclosure should be mandatory.

Disclosing Natural Disasters

Norfolk is a city surrounded by water. In 2014, the Federal Emergency Management Agency expanded the area designated as highest risk for a flood in an update to regional maps, requiring thousands of new homeowners to have flood insurance. The real estate industry worried about the impact on the market. Lawmakers responded.

The region around Norfolk has among the highest rates of annual sea level rise on the East Coast. Rising water and sinking land could push the relative sea level up in some parts by six feet by the end of the century, the United States Army Corps of Engineers estimates. Flood insurance in moderate- to low-risk areas nationally costs more than $200 a year, according to the National Flood Insurance Program, but for properties in flood zones, those rates could rise by as much as several thousand dollars.

Virginia requires real estate agents to reveal whether a property is in a military airplane noise zone, has defective drywall or has ever been used to manufacture methamphetamine. After the flood maps were updated, the industry wondered what new disclosure rules would be mandated. Should homeowners or their agents be required to reveal to potential buyers if the house had been flooded? Should they have to tell how much flood insurance cost and was estimated to rise?

Within a year, state lawmakers passed a real estate disclosure law that the industry hailed as a major step forward. “We are immensely satisfied,” Deborah Baisden, then president of the Virginia Association of Realtors, said of the law.

While the law encourages home buyers to exert due diligence in investigating the risk of living in a flood hazard area, it also explicitly states that the seller of a home is not obligated to disclose whether the home is in a zone that FEMA regards as high risk.

Some city officials said the law did not go far enough. “It’s a nondisclosure disclosure,” Meg Pittenger, an environmental manager for the city of Portsmouth, Va., told a reporter for The Virginian-Pilot. She added that it should have required sellers or agents to inform prospective buyers whether a property lies in a flood zone.

Flood risks are easily overlooked because past flood damage often goes unreported and, as in Virginia, the burden of discovering it falls to the buyer. LexisNexis, a news and legal research company, can supply sellers a report with the history of flood claims on the property, but buyers usually do not know to ask for it. FEMA collects information on federal insurance claims for homes nationally, but the agency has been reluctant to make it public for privacy reasons.

States and local real estate agents are handling disclosure differently. In Florida, real estate agents have to notify purchasers if a property is subject to natural hazards, but the law applies only to a limited area along the Florida coast and has no penalties for noncompliance. And in 2010 lawmakers stripped the requirement to disclose a property’s windstorm mitigation rating.

California, Washington and Pennsylvania, on the other hand, require the disclosure of past flooding or susceptibility to future flooding. In New York, sellers are required to disclose whether a property sits in a flood plain. “It may be a matter of life and death,” said State Senator Stewart Greenleaf of Pennsylvania, who sponsored a state disclosure rule that became law this year.

Some real estate agents around Boston have begun taking prospective buyers to newly repaired multimillion-dollar sea walls built to protect homes from storm damage. They also have begun to encourage clients to increase the marketability of their properties by installing storm-resistant technology, including steel beams and window flaps that allow water to flow in and out of a basement during a flood.

Not everyone favors more disclosure, said Daren Blomquist, the senior vice president of communications at Attom Data Solutions, the real estate data tracking firm that serves brokers, lenders and insurers. After strong objections from real estate companies, which threatened to stop providing data, his firm took down its web page that integrated real estate listings with plot-by-plot information about the risks of floods, hurricanes, wildfires and other natural hazards.

"The pressure was intense," he said, adding that the company still provides this information on separate web pages.

Banks and Insurers Try to Adapt

It is not just property owners, buyers and sellers who are struggling to estimate the potential financial impact of climate change on the real estate market. These risks compound as individual mortgages get bundled and sold as securities. In his April report, Mr. Becketti, the Freddie Mac economist, emphasized how difficult it was to predict whether the bubble in coastal real estate would slowly deflate or suddenly pop.

"Will the value of the house decline gradually as the expected life of the house becomes shorter?" he wrote. "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?"

The real estate and mortgage markets have been slow to confront climate change, said Albert Slap, an environmental lawyer and the president of Coastal Risk Consulting, a company that advises communities on how to prepare for sea level rise. Most buyers of securities, for example, underestimate the risk in their portfolios by relying on FEMA flood maps, he said. Strictly backward looking, these maps are based on floods that have already occurred.

To make matters worse, the National Flood Insurance Program is more than $20 billion in debt. After several major coastal storms, Congress tried to fix the program, passing a law in 2012 requiring that insurance premiums be recalculated to accurately reflect risk. Coastal homeowners rebelled, arguing that the legislation made insurance unaffordable, and in 2014 Congress repealed parts of the law.

George Kasimos, a real estate expert in Toms River, N.J., said homeowners had good reason to react. “A homeowner may be approved for a $300,000 mortgage with a $3,000 a year flood insurance premium,” he said, but the same person’s loan application would most likely be rejected with a $10,000 flood insurance premium. As insurance prices rise, some home purchases will become cash only, squeezing more middle-class and lower-income buyers out of the market.

The North Carolina shore has been especially popular among baby boomers along the East Coast looking for an affordable retirement option.

David Jacobs, 54, said he expected that his home — about 50 feet from the water in Wrightsville Beach, N.C. — will be washed away soon enough. “It pains me to think my children and grandchildren may not be able to enjoy it,” he said, adding that his flood insurance is now about $400 more per month than it was when he moved there in 2013.

Economists have also called for reporting rules so securities investors would know what portion of their bundled mortgages includes high risk from climate change, like properties in coastal regions, river flood plains, flammable canyons and mountainsides, earthquake zones, tsunami washout zones and tornado alleys.

“Coastal mortgages are growing into as big a bubble as the housing market of 2007,” said Philip Stoddard, the mayor of South Miami. But this time, he said, there will not be a rebound because the waters will not recede and properties will eventually lose all of their value.

Politicians are more focused on keeping developers calm and reassuring people that technological solutions will save the day, he said, which plays into an expectation, especially among the wealthiest homeowners, that the government will bail them out if property values crash.

Riding Out the Storm

Coastal homeowners are reluctant to leave. Robert Meyer, the co-director of the Risk Management and Decision Processes Center at the Wharton School of the University of Pennsylvania, has been using web surveys to assess the willingness of South Florida residents to pay higher taxes for climate-change upgrades rather than move.

“They show a remarkable willingness to stick it out,” Mr. Meyer said. His study found that by 2050 people would still be living in the riskiest areas and would have incrementally paid billions of dollars for adaptation measures.

Despite the slowdown in home sales, many flood-prone cities are still growing. Skyscrapers and new apartment buildings are going up all around Fort Lauderdale. The local chamber of commerce says the city expects to add about 50,000 people in the next 15 years and currently lacks housing to accommodate them. In Miami, much of the new construction consists of luxury condos aimed at a large number of cash buyers from Russia and Latin America.

Nationally, median home prices in areas at high risk for flooding are still 4.4 percent below what they were 10 years ago, while home prices in low-risk areas are up 29.7 percent over the same period, according to the housing data.

Chris Bergh, the South Florida conservation director at the Nature Conservancy, said he was worried because his house on Big Pine Key was just over a half-mile from the beach and only about five feet above sea level.

“In planning for my 7-year-old child’s future,” he said, “I can’t count on him inheriting a valuable piece of property on Big Pine Key.”

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