

## SFA Research Corner

### Natural Disasters and Their Impact on Securitization

October 24, 2024



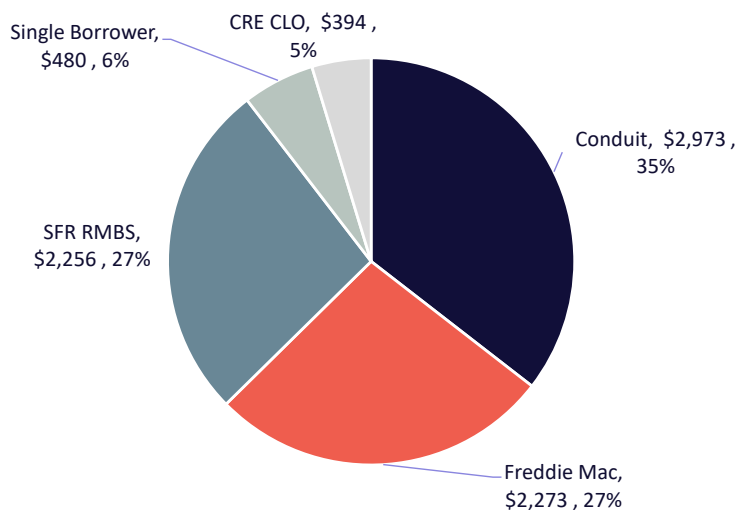
### Natural Disasters and Their Impact on Securitization

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Hurricanes Helene and Milton wreaked havoc across four states. Hurricane Helene caused catastrophic inland flooding and destructive storm surge along most of Florida’s Gulf Coast, with total wind and flood damage estimated between \$30.5 billion and \$47.5 billion, according to [CoreLogic’s Hazard HQ Command Central](#).™ Two weeks later, Hurricane Milton added to the devastation, affecting 850 square miles of Central Florida and resulting in estimated damages between \$21 billion and \$34 billion. Beyond the tragic loss of life, natural disasters like hurricanes, earthquakes, and wildfires often lead to localized economic disruptions, such as job losses and reduced activity, which can consequently drive up delinquencies and defaults. Understanding how these risks affect different asset types is crucial for maintaining the stability of securitization pools.

A recent [KBRA](#) report identified 305 KBRA-rated deals with total loan balance exposure of \$8.4 billion across 11 Florida counties at risk from Hurricane Milton. These deals included conduit CMBS deals backed by diverse portfolios of commercial real estate loans, single-asset, single-borrower (SASB) CMBS backed by a single large loan property or small portfolio of loans from the same borrower, multifamily loans from Freddie Mac, and CRE CLOs backed by short-term loans. Included in KBRA’s list were ten Single Family Rental RMBS transactions.

#### Hurricane Milton’s Impact Across CRE-related Asset Classes



Source: [KBRA](#)

[Moody's](#) also called out Single Family Rental RMBS in their recent report, noting almost all of these deals have greater than 10% exposure to properties in declared disaster areas. However, the agency expects delinquencies and vacancies to recover once repairs are made. Moody's reports that 7% of loans in its rated-RMBS universe are linked to properties in FEMA-declared disaster areas. The rating agency anticipates minimal impact on consumer ABS deals due to the "significant geographic diversity" in most of these transactions.

### **The Role of Geographic Diversification**

Geographic diversification is one of the most effective ways to mitigate the impact of localized natural disasters. Consumer ABS transactions typically benefit from geographic diversification. Lenders with a national footprint often structure securitizations with loans spread across diverse regions. For instance, in a recent \$2 million auto loan ABS transaction, the largest concentration of loans was in California (17%), followed by Texas (10%) and Florida (7%). No state exceeded 19% across the issuer's 11 transactions, safeguarding cash flow from potential regional disasters.

### **Impacts on Unsecured vs. Secured Assets**

Natural disasters impact securitization differently depending on whether the assets are secured or unsecured. Unsecured assets, such as personal loans and credit cards, which are common in consumer asset-backed securities (ABS) transactions, rely solely on the borrower's ability to make payments. When disasters cause financial hardship, borrowers may struggle to meet their obligations, leading to higher rates of delinquencies and defaults.

In contrast, secured assets, such as auto loans and mortgages, found in both consumer and commercial ABS, as well as in commercial and residential mortgage-backed securities (CMBS and RMBS), are backed by collateral like homes, vehicles, or businesses. Natural disasters can cause physical damage to this collateral, lowering recovery values and further disrupting cash flows for these securitizations.

### **Mitigation Strategies for High-Risk Areas**

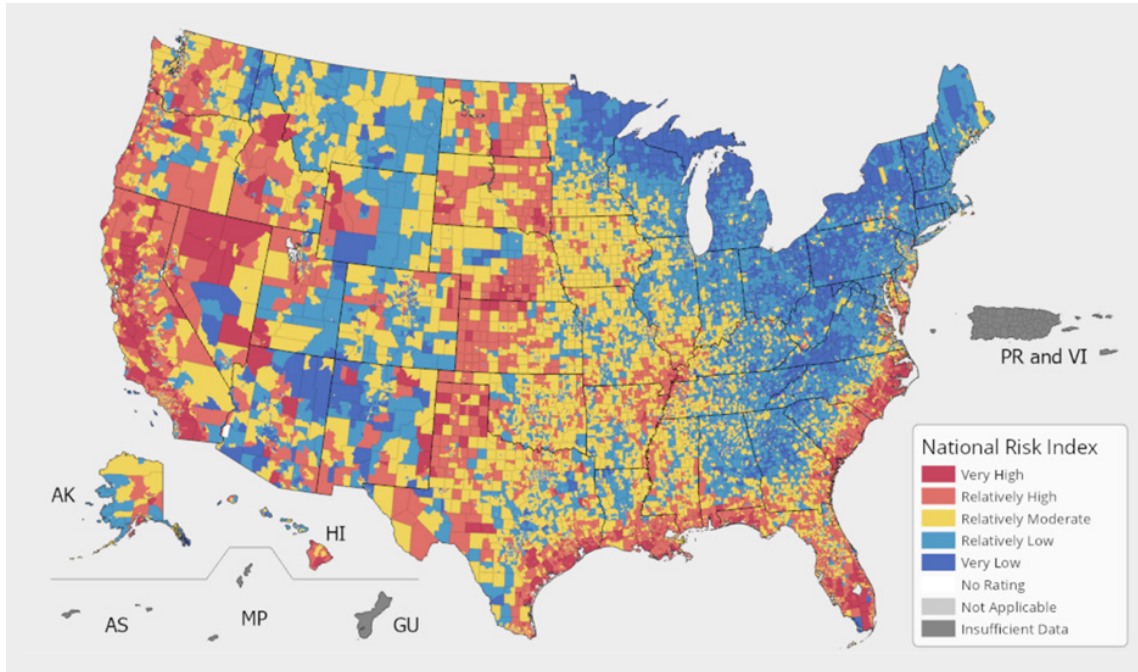
In securitizations where geographic concentration is unavoidable, various strategies are employed to mitigate exposure to high-risk regions. One approach involves insurance protections, where required policies such as comprehensive and collision insurance for vehicles or comprehensive property and business interruption insurance can cover damages. This coverage preserves the income stream when assets or operations are affected by disasters.

Structural safeguards are another important strategy. Securitization structures often include features like reserve accounts, subordination, and excess spread to mitigate risks associated with increased defaults and disrupted cash flow. In commercial and residential mortgage-backed securities (CMBS and RMBS), servicer advancements can provide liquidity during periods of disruption, ensuring smoother cash flow management.

Analytics play a crucial role in these strategies as well. Data platforms like [CoreLogic's Hazard HQ](#) and [FEMA's National Risk Index](#) assess natural disaster risks, helping market participants evaluate potential impacts on asset performance and manage risk more effectively. For example, CoreLogic's [2024 Hurricane Risk Report](#) identified that across the U.S. Gulf Coast and East Coast, over 32.7 million residential properties, with a total reconstruction cost value of \$10.8 trillion, are at moderate or greater risk of hurricane wind damage. Additionally, approximately 7.7 million properties, with a reconstruction cost value of \$2.3 trillion, are at risk of storm surge flooding. As George Gallagher, Principal in CoreLogic's Climate Risk, Natural Hazard, and Spatial Solutions Group, explains, "In the building physical risk context, building and location attributes matter: what is the age/use of the facility, what is the construction type, what is the first floor height, what proximate hazards (water catchment areas for flooding, native plants for wildfire fuel sources, roof age and condition for Hail & wind impacts), what is the existing frequency and severity of individual and combined perils, and their anticipated change over time? Modeling hazard impacts is an exercise in reducing uncertainties: granular property and location-specific attributes reduce the uncertainties, leading to more refined and defensible outcomes."

By utilizing these mitigation strategies and analytical tools, securitizations can more effectively manage the challenges posed by natural disasters, protecting cash flows and ensuring the stability of their asset pools.

**FEMA's National Risk Index: A Dataset and Tool Highlighting  
U.S. Communities Most at Risk for 18 Natural Hazards**



Note: The National Risk Index is a dataset and online tool to help illustrate the United States communities most at risk for [18 natural hazards](https://hazards.fema.gov/nri/learn-more). It was designed and built by FEMA in close collaboration with various stakeholders and partners in academia; local, state and federal government; and private industry. Source: <https://hazards.fema.gov/nri/learn-more>