Ceres Accelerator
FOR SUSTAINABLE CAPITAL MARKETS

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Federal Housing Finance Agency
400 7th Street, SW
Washington, D.C. 20219
Via FHFA Open for Comment or Input Page

Re: Response to RFI on Fannie Mae and Freddie Mac Proposed 2025-2027 DTS Plans

Dear Ms. Barringer:

It is a pleasure to submit comments on behalf of Ceres and the Ceres Accelerator for Sustainable Capital Markets. Ceres is a nonprofit advocacy organization with over 30 years of experience working to accelerate the transition to a cleaner, more just, and sustainable world. Our Investor Network currently includes over 220 institutional investors that collectively manage over $44 trillion in assets. Ceres is a founding partner of the Net Zero Asset Managers Initiative and the Paris Aligned Investor Initiative, which supports investors in aligning their investments and portfolios with the goal of a net zero emissions economy by 2050 or sooner. Our Company Network includes 50 major corporations representing industries and sectors across the economy with whom we work on an in-depth basis on climate strategy and disclosure, among other issues. Our Policy Network includes some of the most well-known brands in the U.S. with whom we work on a range of state and federal policy issues.

The Accelerator aims to transform the practices and policies that govern capital markets by engaging federal and state regulators, financial institutions, investors, and corporate boards to act on climate change as a systemic financial risk. The comments provided herein represent only the opinions of Ceres, and do not necessarily infer endorsement by each member of our Investor, Company, or Policy networks.

I. INTRODUCTION

Climate-related financial risk – which represents the potential financial losses associated with physical and transition risks resulting from climate events – pose significant financial risks to the nation's housing and mortgage markets. Both physical and transition risk can result in significant financial losses for the Enterprises and the communities they serve, jeopardizing affordable housing goals. In 2023 alone, 2.5 million people lost their homes temporarily or permanently due to climate events such as fires, floods, and droughts. Experts estimate that nearly half of all U.S. homes will face severe or extreme damage from environmental and climate risk in 2024, and that

7.5 million people will leave areas with current and emerging high exposure to climate risk in the next 30 years.

Climate risk also exacerbates existing financial and environmental inequities that underserved communities face. Due to decades of systemic discrimination, redlining, and underinvestment, vulnerable communities – including low- and moderate-income (LMI) communities and communities of color[1] – disproportionately bear the economic burdens of climate impacts on housing.[2] These communities are often situated in areas more susceptible to natural disasters which further impacts the availability of mortgages and insurance, have fewer resources to invest in climate-resilient infrastructure or to recover from climate-induced damages, and face higher energy burdens. These events further damage the affordable housing supply – which is at increased risk from climate events such as sea level rise, storms, and flooding[3] – leading to slower repairs, a widening racial wealth gap, and even the inability to rebuild new or build new homes where funding is scarce and rehabilitation and resiliency costs are high.[4]

Additionally, climate-related risks could impact Enterprise liquidity. Delinquency rates for high debt-to-income ratio loans are lower for homes with higher energy efficiency ratings, with an even larger impact during a period of market turbulence and high delinquencies. Increasing energy and

[1] *See* REPORT ON CLIMATE-RELATED FINANCIAL RISK, FIN. STABILITY OVERSIGHT CNCL. (Oct. 2021), https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf#page=24; *see also* Isabelle Anguelovski et al., WHY GREEN "CLIMATE GENTRIFICATION" THREATENS POOR AND VULNERABLE POPULATIONS, PNAS (2019), https://www.pnas.org/doi/10.1073/pnas.1920490117.

[2] *See, e.g.*, Laura A. Bakkensen & Lala Ma, SORTING OVER FLOOD RISK AND IMPLICATIONS FOR POLICY REFORM, J. OF ENVT'L ECON. & MGMT. (July 2020), https://www.frbsf.org/wp-content/uploads/sites/4/Bakkensen_Ma_2020.pdf; Patrick Sisson, *In Many Cities, Climate Change Will Flood Affordable Housing*, BLOOMBERG (Dec. 1, 2020), https://www.bloomberg.com/news/articles/2020-12-01/how-climate-change-is-targeting-affordable-housing; Daniel Cusick, *Past Racist "Redlining" Practices Increased Climate Burden on Minority Neighborhoods*, SCI. AM. (Jan. 21, 2020), https://www.scientificamerican.com/article/past-racist-redlining-practices-increased-climate-burden-on-minority-neighborhoods/; Brad Plumer and Nadja Popovich, *How Decades of Racist Housing Policy Left Neighborhoods Sweltering*, NY TIMES (Aug. 24, 2020), https://www.nytimes.com/interactive/2020/08/24/climate/racism-redlining-cities-global-warming.html; Sarah Kennedy, *The link between racist housing policies of the past and the climate risks of today*, YALE CLIMATE CONNECTION (Mar. 18, 2021), https://yaleclimateconnections.org/2021/03/the-link-between-racist-housing-policies-of-the-past-and-the-climate-risks-of-today/.

[3] *See, e.g.*, Maya K Buchanan et al., SEA LEVEL RISE AND COASTAL FLOODING THREATEN AFFORDABLE HOUSING, ENVT'L RES. LETT. (2020), https://iopscience.iop.org/article/10.1088/1748-9326/abb266/pdf; Guillermo Ortiz et al., A PERFECT STORM: EXTREME WEATHER AS AN AFFORDABLE HOUSING CRISIS MULTIPLIER, CTR. FOR AM. PROGRESS (2019), https://www.americanprogress.org/article/a-perfect-storm-2/.

[4] *See, e.g.*, UNDERSTANDING CLIMATE RISK: WHAT WE LEARNED ABOUT THE IMPACT OF CLIMATE RISK ON AFFORDABLE HOUSING DEVELOPMENT, FED. RES. BANK OF SAN FRAN. (Mar. 2022), https://www.frbsf.org/our-district/about/sf-fed-blog/understanding-climate-risk-impact-on-affordable-housing-development/; Daniel McCue, *Headlines from the 2019 State of the Nation's Housing Report*, JOINT CTR. FOR HOUSING STUD. OF HARVARD U. (Aug. 7, 2019), https://www.jchs.harvard.edu/blog/headlines-from-the-2019-state-of-the-nations-housing-report.

climate resiliency can thus help reduce significant financial risks and enhance stability across the Enterprises' portfolios. Further, if a large number of homes are damaged or destroyed by a climate-related event, the supply of homes available to serve as collateral for MBS could decrease, which could reduce the liquidity of the market and impact the pricing of MBS. Such concentration risk has already led to two credit unions closing due to climate risk. Climate-related risks could even impact the broader housing market and the availability of credit for homebuyers if a region experiences frequent flooding or other climate-related events, and lenders – and insurers – become more hesitant to lend in that region, making it more difficult for homebuyers to obtain mortgages and impacting the availability of credit in the market.

II. RESPONSE TO QUESTIONS

Ceres participated in the July 17 public listening session on the Affordable Housing Preservation Proposed Plans. Our responses below reflect that testimony.

A. Question 1: Do the proposed 2025-2027 activities and objectives address the most relevant obstacles to liquidity in the applicable underserved market?

The inclusion of energy efficiency and resiliency improvements are an important part of addressing obstacles to liquidity in the affordable housing preservation market. Climate risk can result in significant financial losses for both the Enterprises and the communities they serve, jeopardizing affordable housing goals.

Energy efficiency improvements deliver savings and resiliency to homeowners and residents by decreasing utility payments and total housing costs as well as physical safety. Utilities are one of the highest monthly home costs, particularly for first-time, low-income, and BIPOC households. HUD and USDA found that more energy efficient homes would save an average of almost $1,000 in single-family home energy bills each year. These improvements also reduce risk to the Enterprises by lowering delinquency rates, making homeownership more affordable, and increasing the proportion of new issuance loans with energy and water efficiency improvements, reducing its interest rate exposure.

The proposed DTS plans offer some encouraging and ambitious objectives, including Fannie Mae offering two cost-benefit analyses of key energy efficiency and resiliency upgrades, launching a pilot based on the energy efficiency and resiliency work, and partnering with nonprofits to deliver technical assistance to organizations on how to preserve affordable housing through increased resilience to severe weather events; and Freddie Mac expanding the purpose and content of DPA One to include information on government tax credits and other incentives for energy and water efficiency improvements. These activities and objectives can help the Enterprises lower the barriers to financing energy efficiency and resiliency improvements, which can otherwise make lending in these markets less attractive.

B. Question 2: Are the proposed objectives likely to increase liquidity in the applicable underserved market?

The proposed energy efficiency and resiliency improvements are likely to increase liquidity in the affordable housing preservation market through reducing default risks by lowering utility costs and making homes more resilient to natural disasters, which in turn makes loans more attractive to lenders. Green bonds and other sustainable investment products that finance energy efficiency and resiliency improvements also appeal to a growing segment of investors focused on environmental, social, and governance criteria, increasing sources of funding and enhancing Enterprise liquidity. Further, the use of incentives like the Inflation Reduction Act's (IRA) Greenhouse Gas Reduction Fund (GGRF) could further encourage lender participation. To increase the effectiveness of these objectives in increasing liquidity, the Enterprises should commit to raising loan purchase targets, scaling these initiatives, and expanding efforts to additional underserved markets.

C. Question 5: Are there other activities and objectives the Enterprises should consider adding to their Plans for the manufactured housing and affordable housing preservation markets to address access to liquidity and other housing finance needs in those markets?

Like energy efficiency improvements, home hardening and other weather- and natural disaster-resiliency efforts reduce burdens on homeowners and renters. Natural disaster preparedness and weather- and climate-resiliency help preserve and support sustainable and resilient residential housing and community development, but require sufficient liquid resources. Proactive improvements and financing play a critical role in helping LMI and other vulnerable communities prepare for, adapt to, and withstand natural disasters and weather- and climate-related risks. Pre-disaster evaluation, planning, and investment can help mitigate both future physical impacts of climate events (i.e. reducing flooding) and associated financial burdens (i.e. lower energy and rehabilitation costs). Both of these benefits support the Enterprises' duty to serve the affordable housing preservation market, and are incorporated to some extent in their Equitable Housing Finance Plans.

We therefore urge the Enterprises to incorporate climate resiliency activities and objectives similar to their energy and water efficiency activities and objectives for both single- and multifamily properties in the housing preservation market. Freddie Mac should include and Fannie Mae should update (Activity J) their DTS plans to incorporate activities and objectives that increase the financing of resiliency improvements; reduce the costs of those improvements to homeowners and renters through consumer tools, new programs, and loan products; and increase the purchase of mortgage loans that finance those improvements or refinance existing resiliency improvement debt.

The Enterprises should also consider several additional activities to enhance access to liquidity and address housing finance needs in the affordable housing preservation market:

- Community Reinvestment Act (CRA) collaboration: Work more closely with banks subject to the CRA – which now includes natural disaster and weather resiliency community development activities – to encourage investment in affordable housing that incorporates energy efficiency and climate resilience while providing CRA credit.

- Government programs and incentives: Work with institutions to leverage the IRA's GGRF incentives, State Energy Offices that offer rebate programs, and other available incentive programs that lower the upfront costs of improvements, encouraging affordable housing developers, owners, and lenders to finance these projects and increasing the flow of capital into the affordable housing market.

- Green loan products: Broaden the range of green loan products available for both single- and multifamily properties to include a wider variety of resiliency improvements that will increase the financing; reduce the costs of those improvements to homeowners and renters through consumer tools, new programs, and loan products; and increase the purchase of mortgage loans that finance those improvements or refinance existing resiliency improvement debt.

- Technical assistance for small lenders: Provide more technical assistance and tools to small and community lenders to help them better understand and finance energy efficiency and resiliency projects in affordable housing, particularly in high-risk areas.

- Borrower outreach: Develop a more detailed plan to reach DTS-eligible homeowners at the time or purchase or refinance to provide assistance in utilizing IRA and other programs and ensure maximization of these incentives.

D. Question 6: Should the Enterprises adjust the methodology used to set loan purchase baselines for 2025-2027, given current market conditions including elevated interest rates?

While interest rates are currently elevated, DTS priorities make up a small fraction of Enterprise portfolios compared to the broader affordable housing goals requirements. Market conditions are also comparable to when the 2023 targets were set, which were set factoring in the market changes we now see, and energy burdens in affordable housing remain significant, as do the associated risks to the Enterprises. Failure to adequately address these conditions could exacerbate default risks and increase the long-term costs associated with maintaining affordable housing stock.

We therefore urge the Enterprises to increase their (Activity F, Objective 2; and Activity 1, Objective A) energy and water efficiency loan purchase targets to 500 by 2025 and increase yearly by 100. We likewise urge the Enterprises to identify an additional 5-10 underserved high energy

burden markets and focus on at least five of these for the 2025-27 plans. Market conditions are strong enough to achieve these relatively modest loan purchase targets, particularly when taking into account CRA incentives, GGRF incentives, State Energy Offices that offer rebate programs, other available incentive programs, and the growing investor demand for sustainable and green financial products. These targets will help sustain momentum in the market as well as safeguards for the Enterprises – broadening the potential purchase market, enhancing appreciation, and improving loan performance.

The DTS methodology should also include regular reporting on progress toward loan purchase targets, with a clear process for making adjustments as needed. Transparency in how targets are set and adjusted will build confidence among stakeholders and ensure that the methodology remains aligned with broader affordable housing goals and market conditions.

E. Question 7: Are there other market conditions that FHFA should consider when assessing the proposed activities and objectives?

When assessing the proposed activities and objectives, the FHFA should consider the increasing frequency and severity of climate events, including how climate risk might influence migration patterns and housing demand in certain areas. Such an assessment should also incorporate review of the availability and affordability of mortgage and property insurance may impact Enterprise liquidity and credit risk – including consumer understanding of their risk and what is/is not covered in their policies.

Potential changes in federal, state, and local regulations regarding building codes, energy efficiency standards, zoning laws, and public disclosures could also impact the proposed activities and objectives. The FHFA is reviewing the impacts these changes may have on the Enterprises, and should extend those deliberations to their assessment of the Enterprises' proposed DTS activities and objectives.

F. Question 8: Are there any safety and soundness concerns related to the proposed activities and objectives?

Climate risk can present safety and soundness concerns that the proposed energy efficiency and resiliency improvement activities and objectives may help alleviate:

- Asset quality: enhancing property resilience through energy efficiency and adaptation measures can help maintain asset quality as physical risks deteriorate property values and transition risks shift business models and available products.
- Capital adequacy: increased defaults, asset devaluations, or operational challenges may lead to significant financial losses that could strain capital reserves of the Enterprises if properties are not made more resilient to climate impacts.

- Credit risk: making properties more energy efficient and resilient to climate-related events can reduce the likelihood of defaults by lowering utility costs, reducing physical damages, and protecting property values.
- Earnings sufficiency: making properties more energy efficient and resilient to climate-related events can mitigate increased costs associated with managing climate risk – such as higher insurance premiums or losses from defaults – and increase earnings from green financial products.
- Liquidity risk: improving home energy efficiency and climate resiliency can help reduce the risks from climate-related events that may increase delinquencies and devaluation and decrease supply that can serve as collateral for MBS.
- Market risk: as consumer and investor demand increases for environmental, social, and governance products, green bonds and other sustainable investment products that finance energy efficiency and resiliency improvements can increase sources of funding and reduce exposure to asset loss.

III. CONCLUSION

We thank the FHFA for the opportunity to comment on the Enterprises' 2025-2027 DTS Plans. We believe the continued inclusion of energy efficiency and resiliency improvements targets and objectives is imperative to ensuring underserved and disadvantaged communities have sustainable access to safe and affordable housing. We would be pleased to discuss any questions you may have on our feedback; please contact Kelsey Condon at kcondon@ceres.org.

Sincerely,

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