

The Hidden Risk to Americans' Financial Health

We hear about market ups and downs, shifts in the inflation rate and a lot of scary health risks. But nobody seems to be talking about the biggest single financial pitfall that may be looming for many Americans. According to a recent report on climate risk—with the increasing prevalence of wildfires, floods, hurricanes, tornados, damaging winds and other climate-related catastrophes—more than \$12.7 trillion worth of U.S. real estate is now in significant danger of destruction. The survey also found that as many as one in seven homes are no longer insured for these catastrophes.

The total loss of home equity would likely wipe out many Americans. Even those who do happen to have property and casualty insurance may now be dramatically underinsured—meaning that they, too, could be wiped out by their share of repair costs should their home be damaged by flood, fire, wind or storm.

Nationwide, insured losses are rising by 5% to 7% a year, and of course that means that homeowners insurance premiums are rising proportionately, causing yet another erosion of peoples' nest eggs. And that's if the owner can find coverage. A number of insurers have stopped writing policies in high-climate-risk states like California and Florida, and most policies now come with added exclusions, gaps and surcharges. Traditional homeowners' insurance often excludes the most prevalent disasters: floods, hurricanes, wildfires and wind damage. Those protections require separate policies, higher deductibles or added endorsements.

Even if the uninsured homes don't suffer a climate-related catastrophe, the home value could still be diminished or vanish altogether. In many homes where the mortgage has been paid off, the mortgage payment that used to include homeowners' coverage no longer does. The owner, aghast at the premiums, decides not to renew. Meanwhile, construction costs continue to rise faster than the inflation rate. Materials costs are now more than 40% higher than they were in 2020, and labor shortages are starting to crop up for homebuilders. By one estimate by the Associated Builders & Contractors, the industry is going to need to attract 499,000 new workers to meet demand, and labor costs are accelerating.

After 10 or 20 years of whistling past the graveyard—of taking on the risk of a catastrophic loss with no consequences—the owner decides to sell.

But guess what? The premiums are now so high that a potential buyer will only make an offer at a steep discount—and if coverage is unavailable or the home is in a floodplain or at high risk of wildfires, there may not be a market at all for what the owner had counted on as a store of value for his/her retirement.

The survey, by Realtor.com, concludes that the growing climate risk and rising insurance costs are posing a threat to the entire housing market, as uninsured losses turn homes into distressed properties and leave neighborhoods with empty, damaged houses that drag down values.

There is no easy remedy for this hidden risk to Americans' prosperity. It is becoming increasingly important for homeowners to become astute shoppers for their insurance coverages, and to understand the unique risks in their home location. What was once a routine part of owning a home has become much more complicated, and what was once people's most valuable investment is increasingly in danger.

Sources:

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