

# Freddie Mac Single-Family Home Starts Here Podcast Episode Transcript:

Making the GreenCHOICE to Drive Home Affordability

**Announcer** [00:00:01] Welcome to the Freddie Mac Single-Family Home Starts Here podcast, your connection to all the latest industry trends, insights and points of view on the mortgage market from Freddie Mac leaders and other industry experts.

**Mike Tsikoudakis** [00:00:14] Hello and welcome to this special episode of The Home Starts Here podcast. My name is Mike Tsikoudakis, from Freddie Mac and I'm your host today. I'm a content strategist here at Freddie and I lead our thought leadership editorial efforts for Single-Family and I'm excited about today's topic because it's something we've explored before, but now it's more timely than ever. And I have two great guests that will shine some light on the topic for us with new actionable perspectives. Since Earth Day, just past, we're exploring energy efficiency trends for homeowners and potential borrowers. Freddie Mac believes that reducing home utility costs places families in a better financial situation and helps preserve home affordability over time. Since the first Earth Day in 1970, changes in building codes have made homes much more efficient, cutting energy use by forty seven percent. But homeowners may still be paying more for utilities than they should. This can be due to poor insulation, inefficient lighting fixtures, air leaks and outdated heating and cooling systems. By reducing these costs through energy efficiency upgrades, homeowners could save money and be more comfortable, especially in older homes. So why is this important to talk about today? Well, with the ripple effect of the Covid-19 pandemic that is spiking residential energy consumption and utility expenses, it also is introducing potential problems to energy suppliers and distributors, as we saw in Texas earlier in the year. So today, we're going to learn more on how lenders can assist consumers in making simple, budget friendly, sustainable home upgrades. We're joined today by Simone Beaty, affordable lending senior director at Freddie Mac Single-Family, and our special guest, Steve Baden, executive director at RESNET. I would love to hear about who they are and what they do. Simone, let's start with you.

**Simone Beaty** [00:02:00] Thank you, Mike. So, I work in the Single-Family Client and Community Engagement Group, and I lead the team that develops the strategies in support of underserved markets as part of our Duty to Serve initiative. And energy efficiency is actually one of those markets. So, this topic is definitely top of mind for us.

**Mike Tsikoudakis** [00:02:21] Absolutely. Thank you, Steve. Can you give us a bit of background about yourself and also a little bit about what RESNET does?

**Steve Baden** [00:02:30] Yes, I'm the executive director of RESNET, I was one of the founding members of RESNET and it's very appropriate today with Earth Day that you've invited me here. RESNET was actually founded as a partnership between the mortgage industry, state energy offices and rating programs across the country. Its purpose was to provide mortgage lenders a way to easily determine the efficiency of a home. The formation was guided by a mortgage industry steering committee that was co-chaired by the then CEO of Freddie Mac and the president of the Mortgage Bankers Association of America. Our product is the HER's rating and 'HERS', which stands for home energy ratings. What it does is it involves an inspection and testing and labeling of a home by a certified professional that provides a number of things that a consumer and lender can use. First, it provides a score which is akin to an MPG rating, if you will, for a home. It also includes calculated energy use and savings. Suggestions on what a home can be improved in economic analysis and calculated savings. It also includes a calculation of the carbon that the home produces and how much carbon can be saved by making improvements. In 2020 there was almost 300,000 homes rated in the U.S., which put us over the 3,000,000 mark in terms of the homes that have been rated through the RESNET standards.

**Mike Tsikoudakis** [00:04:03] Thank you for that background, Steve. So, I'd like to start out our discussion today talking about energy audits and Simone I'll turn to you first. What are energy audits? What do they mean for our listeners?

**Simone Beaty** [00:04:17] Yes, that's a great question in terms of what it means to our listeners is, to the extent that a consumer has not had an energy assessment already produced on their home, an energy audit essentially tells a property owner or a building owner how efficient their building is or their home is or whether they meet a certain standard of efficiency, right? So, there could be a certification that says, hey, you are deemed energy efficient because you have a certain certification now applied to your property because of the way it was constructed or improved. Or you can have an assessment done that tells you exactly how efficient or not your property is at a specific point in time based on certain standards and in comparison, to a home that may not be rated. So in terms of what it means to both consumers and in the lending community, it gives us an opportunity to identify in the marketplace homes that have, you know, some sort of efficiency or whether it be energy or water that basically helps the consumer reduce the amount of utilities that they're consuming on a monthly or on an annual basis. That information is important as we look to, both the lending and the billing community to build to a higher standard of efficiency. If the ultimate goal is to have a reduction on fossil fuel reliance and a reduction in our overall carbon footprint. And so the only way for us to have a measurement as to whether we are advancing those goals is really to have an energy assessment conducted on a property. Right. So it applies both to the residential side and also the commercial side as well. But for Freddie Mac and for the purposes of this podcast, focusing predominantly on Single-Family properties for which that is a huge market.

**Mike Tsikoudakis** [00:06:17] Got it. That's really interesting. And I'm curious, you know, energy audits are obviously very, very important. What's the difference between an energy rating? And I'm throwing that out there to you, Simon or Steve, to kind of give us the difference between those two things?

**Steve Baden** [00:06:32] The differences, if you will. I'll use this metaphor of the health industry. An energy audit is a quick survey, somewhat inexpensive, and it just gives you an overall sense of what the energy use of the home is. It's akin to an annual checkup going to your doctor. And so, this gives the consumers an idea of how efficient the home, where the problem areas are and some things that they can look to do it. Now, a rating is more akin to when you go and get a diagnostic specialist checkup. And what it's intended for and was created is to create a differentiation in the marketplace by which a consumer can compare homes they're purchasing in terms of energy performance and have a consistency way that you can measure homes despite the differences that we have out there in the marketplace. In addition, if a person is looking at a large scale investment in significantly improving their homes, a HER's rating is a lot more detailed and granular and gives a lot more details of all of the options that are available, what the potential savings are, what the potential cost is, and what is the return on investment.

**Mike Tsikoudakis** [00:07:41] Got it, got it. So, in terms of energy audits, who uses these, you know, and when?

**Steve Baden** [00:07:48] It's used for different purposes. A lot of energy audits are driven by utility programs as service to their customers who want to find how their homes waste their energy. They're also used by federal programs such as the Weatherization Program, Home Performance for the Energy Star, that uses the (Department of Energy) DOE home energy score. And then it's also used by and realtors and the housing industry to be able to compare homes on the efficiency and have a comfort level of how much energy that home is using and what improvements can be made.

**Simone Beaty** [00:08:23] What we're also seeing in the marketplace is that home resellers, so existing homeowners are also using it to the extent that local markets are you know, the municipalities are requiring energy assessments on the home as they are reselling the home so that there's disclosure to a prospective home buyer on how energy efficient a home may be that they're purchasing. We're also seeing some market usage in that space as well by consumers requesting those audits as they are putting their homes on the market. So that's a fairly new dynamic.

**Steve Baden** [00:08:56 ] And I think the other thing is important to bear in mind, since we're talking about the mortgage industry here, this should be a tool to lenders because the cost of energy is the highest cost of homeownership outside of the mortgage loan. It's variable, it can be improved. And both tools give a lender and the ability to see what the energy



performance of the home is and how predictable and affordable the home will be to the person buying the home. But more importantly, it's a tool by which they can actually capitalize the potential energy efficiency and make them parts of the mortgage loan, which is the really exciting new developments that's taking place, led by Freddie Mac, of putting these energy considerations as part of the mortgage loan process.

**Simone Beaty** [00:09:39] We launched our green mortgage product a couple of years ago, where it's called Green Choice Mortgage. And essentially consumers can use the offering through a lender to start a green home and a home improvement project or pay off debt for a project they've already completed, as long as that there were energy efficiency components as part of that project. And in terms of an energy assessment an energy assessment is actually part of that product for specific areas of usage. And one of the things that we do to incent lenders to use it is we actually have a credit that essentially offsets the cost of that assessment, because we at the end of the day, we don't want a lender to not choose the that this type of financing that could be so beneficial if they are worried about additional costs incurred because of an energy assessment. The other thing I wanted to mention is for listeners wanting to learn more both the Department of Energy and RESNET, and it has a lot of information available on their website on how these assessments work, where you can find readers. We also did a research paper on rated homes using both of these assessment models. And you can find that information online today on Freddie Mac dot com. The research was called "energy efficiency value added to properties and loan performance". If you want to have a little bit more color on essentially homes that we have noticed that are rating because there are some benefits to consumers, builders, raters, lenders, appraisers. And then also we've noticed that the greener the property, the bigger the premium on those resales.

**Mike Tsikoudakis** [00:11:36] Yeah, that's great. And plenty of good information there on Freddie Mac dot com. I want to turn the conversation to consumer demand for home improvement, especially because of the Covid-19 pandemic are millions of people are working remotely amid the pandemic. Homes have turned into offices, classrooms, multiple devices and gadgets are connected. Steve, has the change in daily life tied to the pandemic, increased energy efficiency awareness or even demand for energy audits? And if they have, how can the mortgage industry and the mortgage professionals, how can they leverage that?

**Steve Baden** [00:12:15] What's happening in two things, interestingly enough. The first is, is that we're spending much more time in our homes now. And when we bought our homes, there were some things that we thought it was what was required. And now that we're spending more time and actually a lot of people working for their homes, and students are going to school via Internet. We're finding that maybe some of those things that we thought was important, it's not so important. And so it's driving two things to happen. One is we're seeing new construction almost exploding. People now want to since they're working from home, the idea of moving to the suburbs is not such a bad idea. They want bigger homes because they got to work there versus live there. And then also they're much more conscious of health and safety and the indoor air quality. The home of the other factor that's going on is we're seeing a big boom in home improvement. And this is where the opportunities lie because we're talking in conjunction with Earth Day. And I think people, when they think of climate change, they're mostly thinking of automobiles and factories. But the truth of the matter is, the biggest contribution of carbon production in the United States are homes. And there are a lot of things now that can be done to lower that profile. In the past five years has been a virtual revolution in products and practices that are now very, very cost effective that people can undertake to cut their energy profile. And this is where I think Freddie Mac and the mortgage lenders come into, because we're seeing a massive number of homes being refinanced because of lowest interest rate or being purchased. And I think that this is a golden opportunity when you're buying or refinancing your home to make a improvements to the home and then paying for it for the mortgage. And because of this, you can afford to be bold. It is possible to reduce your energy consumption by 50 percent. And what's hold it up in America is the fact that people don't have that cash in hand or hesitate of putting it on their credit card. With products such as Freddie Mac has done you're able to when you're actually refinancing your home or making a home improvement to include these energy factors. And then what you find out is you've paid for it at a mortgage interest rate over the period of a mortgage loan, it becomes much much more affordable. And you'll notice that the income that you're making from savings are going to way outweigh the extra cost of the mortgage by making the improvements. So, this is the magic time. We are seeing an uptake of it. Just in 2020, we saw the demand for HER's ratings increased by 26 percent over 2019 and 2019 was a record year.

**Mike Tsikoudakis** [00:14:56] Wow, yeah, that that that definitely strikes a chord for me. I live here in Chicago and to get into the neighborhood with the right school that we wanted, we had to buy a home that was 100 hundred years old. It's more than 100 years old. And I'm looking at improvements every weekend and most of those improvements have to do with energy efficiency. And there is a price tag attached to those. So, kind of wanted to ask if I were looking to do some of these improvements, what would you tell me or what can I do? Can I work with a lender to get help? Simone any any thoughts on that?

**Simone Beaty** [00:15:30] Oh, yeah, absolutely. I think the energy, you know, having a rating helps to understand kind of, you know, set a baseline for your starting point. However, you know, it depends on budget. Right? I think one of the points that Steve mentioned is however big or small that activity ends up being for an individual consumer we would accommodate it. So in terms of what we offer to the lending community is we will support financing of very small amounts of energy improvements, things like weatherization, like basic things that you don't realize impact efficiency that make such a huge difference in the overall to large projects you know, the renewable installations like solar, which is gaining more popularity nationwide. But, you know, basic things are important, programable thermostats, just weatherstripping, changing out, your doors and windows. Things like that you can actually roll it into the mortgage or if you've already done it and you incurred the debt already through credit cards or, you know, unsecured loans, you could also use our offering to essentially pay off that debt as long as you can show that that was the purpose it was used for. But at the end of the day, Steve is right, the low interest rate environment we're in has made the mortgage in terms of the timing of having this offering extremely attractive for home improvement. An energy audit could actually better inform where you should put your dollars to get the savings over time on the home improvement activity that you're doing.

**Steve Baden** [00:17:10] My suggestion for you is particularly looking at a older home, it is well worth your time to get a energy assessment done of your own. We have ways now to actually diagnostic test, we can tell how much energy you're losing in your cracks in your walls. And the average American home has if you put all the cracks and stuff in, it's a hole about the size of a basketball. And those are things you can't see. Those are things we actually now can measure and pinpoint where those are. And what you find is some of the things that you think are the best energy savings things you can do that are the most expensive or may not be the most cost effective. Like air sealing is really inexpensive, but people don't tend to think about it. They think windows or insulation. And so, this is what the specialists will come, look at your particular house, do the diagnostic testing, come up with recommended and within the RESNET HER's rating, it will do the calculations that the mortgage lender needs. It actually complete forms for the appraiser and it would fill out a report then that you could just take to your lender and say that you want to take advantage of a Freddie Mac mortgage product.

**Mike Tsikoudakis** [00:18:18] This is great. So, we talked about the benefits here in terms of energy audits and what are some challenges on expanding the usage of energy audits on Single-Family properties. And Steve, since you kind of have the last word, I'll start with you here, what's your perspective in diversifying usage beyond builders?

**Steve Baden** [00:18:34] That's a good question. I've been in this field for almost thirty years, and this has been a thing that's been hard. There's really two different markets, if you look like there's the new homes. And I think we're increasingly becoming successful— builders are making more efficient homes, builders are increasingly having the HER's rated and are marketing their scores. The tough nut to crack is where most Americans live is an existing home. My opinion is, is that products such as the Freddie Mac product that allows a homeowner to make the improvements and go as far as they think, economically justified and then roll it into the mortgage loan is going to be a game changer. Because then there's a real purpose, because a lot of people, they get an assessment and they look at it and they say, well, that's going to cost five or ten thousand dollars. I don't have that kind of money. Plus, I want to put some kitchen work done, so, we'll put it in a drawer and then it gets forgotten about. But if we can make mechanisms that at times sell or time of refinance or actually coming in and doing an improvement, you can roll it into the mortgage loan, that's the game changer. And that is then going to increase the demand for assessments. It's also going to make the family have more disposable income. And these tough economic times that's important. It's going to help the economy because the energy costs going out the chimney and windows and doors will not be such. And then it's also going to help the environment. We're talking Earth Day here, because it will cut carbon production. So that's the win-win. And I think the biggest factor that can be done is now having the mortgage industry being able to understand and embrace and invest in these improvements that will pay for themselves beginning on day one.



**Mike Tsikoudakis** [00:20:19] Excellent. Simone, any any perspective our thoughts on expanding the usage of energy audits?

**Simone Beaty** [00:20:24] Yeah, Steve, Steve hit the nail on the head. The market opportunity, especially for lenders, looking to see kind of where they should start on the biggest opportunity set is truly existing homes. Right. You know, builders have seen religion on adding, you know, energy efficient components and basically highlighting that as they as they sell homes. But the biggest market that have the benefit of an energy retrofit is on the existing home market. And in order to incentivize the behavior that Steve talk about in kind of using mortgage financing to kind of scale that market in terms of the activity, we really need data. So, you know, the lending community, the investment community really is very data driven on both the opportunity, they want to see the size of the market. And they also want to understand how, you know, existing activity is currently situated in the market and what performance looks like. So, one of the challenges we do experience, because it's still a niche activity today, we see it happening and we see increases. But I think we could further spur the activity generally by having more transparency to the market on what the market looks like, where the activity could be concentrated, where it's not happening, and basically some transparency on efficiency of homes that are out in the market. Right. And so, in order to do that, we at Freddie would need to build out the ability to capture data that we think will be meaningful to the market that would encourage them to participate in it at the mortgage level. the challenge is a bit circular sometimes in order to get that data you need more usage. Right? And as we see more usage, we're able to produce more confident in the information we're supplying to the market. we do have a project currently where we're focusing on just the appraisal form for example. We have a project called the Uniform Appraisal Data Set that essentially informs the data that an appraiser or a home appraiser would provide to us, that tells us the characteristics of the of a property and the value they are attributing to the makeup of a property. But in that today, there isn't a whole lot of information currently on energy or water efficiency, for that matter. And so one of the things that we are eventually will be driving to the market is collection of that information at the property level that will give us data that we can trend, we could trend how values are being impacted by data to the extent that energy efficiency is incorporated at a very specific level. And we can also trend overall mortgage performance as well

**Steve Baden** [00:23:11] Simone mentioned the idea of appraisers. RESNET partnered with the Appraisal Institute and we created a dashboard by which appraisers can go and put a property address in and find out if it was HER's rated or not and if it is HER's rated there, what was the score? What was the projected energy savings when it was rated and who rated it? Also, it gives the ability for a appraiser who wants to do some market comparisons if they have an efficient home. To pull a number of homes in a market that has similar scores by which then you can compare sales data. So, this is kind of the best kept secret out there to the mortgage industry and to the appraisal industry. But that becomes very important because then a lender is even more comfortable if they know the appraisal is able to track that and be able to do the research market data on the return in that particular market on the sales price of the efficient rated homes.

**Mike Tsikoudakis** [00:24:07] that's all very useful information and back to Simone's point. It seems like data is key here. So, we're getting close to wrapping up here. So, I'm going to ask our two guests to look into their crystal balls, what's around the corner in terms of energy efficiency that listeners should be aware of? What's on the horizon that they should prepare for? And Simone I'll turn it to you.

**Simone Beaty** [00:24:28] Yeah, you know, you said it - data is key. And so, for Freddie, we are definitely our eye on the future is building out data capabilities, both collection of it and validation of it. It is going to provide transparency to all facets of the market. Right? All of the ecosystem that is involved in mortgage lending can benefit from having more data in that, you know, having them participate at a greater level will eventually have a domino effect and benefits for the consumer in terms of having affordable financing. So, I think an eye on the future, if I had a crystal ball, I would say this is a market that is growing and, you know, eventually with more data, it could grow by leaps and bounds. I think personally, the sun is shining on this segment and so growth is on the horizon.

**Mike Tsikoudakis** [00:25:19] Absolutely. Steve, what's your what's your prediction or what's your outlook, our forward-looking statement here in terms of energy efficiency?



**Steve Baden** [00:25:26] I'm going to change it a little bit I think the real big key change is going to take place here shortly is water. Water rates, if you notice your water bill lately is increasing exponentially almost, and it's actually water cost. Water and sewer costs are increasingly faster than energy costs and lowest projected that the next two years, a large segment of the Midwest will be facing water challenges. And I think that really, when we look at this, we should be looking at a holistic, as Simone mentioned sometime, not just energy efficiency, but look at utility bills. And I think water is clearly a player in it. And I think that this is another factor that that that could be considered a cost of housing. And RESNET has developed a water efficiency rating system that's sister to energy that can actually go in and be conducted at the same time as a energy rating and does the same kind of information that a a builder can market this home and then the seller can look at more sustainable. But I think the future is water efficiency. And I think that that worked as Simone and Freddie Mac has done, can be easily accommodated to to meet this new concern over water that we're going to be looking at the next couple of years.

**Mike Tsikoudakis** [00:26:43] Thank you. Well, that's all the time we have for today, and I want to thank both of you for joining and thanks to everyone for tuning in today. Please make sure you check out our Single-Family Web site for links to everything that was mentioned in this episode and we appreciate you subscribing, reading and reviewing this podcast wherever you listen. And don't forget to share with your networks. Thank you.

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