How To Protect From A Canadian Housing Implosion

Description

Canadian housing results remain strong, yet there is an underlying fear throughout the financial markets that it's only a matter of time before this trend reverses. By looking back at the recent financial crisis and its U.S. housing market epicenter, we can gain an appreciation for how this turn in Canadian housing might play out.

The Canadian Economy: A Brief Overview

Let's put some things into perspective however before jumping in. Since the lows of 2008, the Canadian economy has done quite well. Unemployment is at 7.1% and showing a slowly declining trend and GDP is showing consistent positive growth. As illustrated in the following chart, GDP per capita has had a strong rebound from the 2010 lows.

Image not found or type unknown
canada gdp per capita

All is not well

While the economy shows several positives, there are also some warning signs to be mindful of. The chart below shows one of the biggest concerns going. Our household Debt/GDP ratio has climbed to the same level achieved in the U.S. prior to the burst of the housing bubble there.

Image not found or type unknown
Canada debt to gdp

In addition, as we illustrated in a past post on this topic, housing price to income ratios are higher in Canada than they've been in either the U.S. or Canada in the past 25 years.

Neither of these stats contribute to a bullish case for housing.

How To Protect The Portfolio

If you believe the Canadian housing market is worth worrying about, there are several ways in which you can protect your portfolio:

1. Diversify Globally

While Canada's markets may be at risk, there's plenty of opportunity to invest outside our borders. Russia's major markets, for example, are down 38% in the last two years and could be ripe for a rebound. One could gain diversified exposure to the Russian market by investing in the **SPDR S&P Russia ETF** (NYSE:RBL). Though volatile, this ETF has a dividend yield of 4.9% and a P/E of 5.6, making it a seemingly attractive option for the long term.

And if country specific risk isn't your thing, you could look towards funds with that have exposure to a variety of markets. The **iShares BRIC Index Fund** (TSX:CBQ) offers investors exposure to companies from Brazil, Russia, India and China and thus helps to spread your risk throughout the globe and far away from the Canadian economy.

2. Bet Against Canada

The most obvious way to protect from the Canadian housing market, however, is to take a small % of your portfolio and bet against our housing market, just as the investors profiled in the Michael Lewis book *The Big Short* did prior to the U.S. collapse.

Betting against the housing market however can be tricky for all but the most sophisticated investors. A more practical approach is to simply avoid the companies that are most exposed to this potential downturn. This means the Canadian financial sector, and specifically **Canadian Imperial Bank of Commerce** (TSX:CM,NYSE:CM), which recently had 37% of total assets in residential mortgages and **Home Capital Group** (TSX: HCG), which has been targeted by hedge fund manager Steve Eisman, one of the investors profiled in *The Big Short.* We commented on Eisman's position in this post from a while back.

Foolish Takeaway

A housing market crash is a scary prospect. However, if you're prepared, not only will you weather the storm, but once it blows over, you'll be in a great position to pick through the wreckage and find fantastic long-term ideas.

For more ideas on how you might avoid a Canadian housing market correction, **click here** to download our special FREE report "**5 Stocks to Replace Your Canadian Index Fund**". One of these 5 just got taken out a huge premium. **Click here** to learn about the 4 that remain. It's **FREE!**

The Motley Fool's purpose is to help the world invest, better. ***Click here now*** *for your free subscription to* ***Take Stock****, The Motley Fool Canada's free investing newsletter. Packed with stock ideas and investing advice, it is essential reading for anyone looking to build and grow their wealth in the years ahead.*

Follow us on Twitter and Facebook for the latest in Foolish investing.

This post was created by Fool contributor Nikhil Shamapant.

Fool contributor Nikhil Shamapant doesn't own shares in any of the companies mentioned. The Motley Fool does not own shares in any of the companies mentioned.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:CM (Canadian Imperial Bank of Commerce)
2. TSX:CM (Canadian Imperial Bank of Commerce)
3. TSX:HCG (Home Capital Group)

Category

1. Investing

Date
2025/08/27
Date Created
2013/07/22
Author
motley-fool-staff