Could This Stock Be the Canary in the Coal Mine for the Canadian Housing Sector?

Description

Over the summer, the Canadian housing sector had started to show signs of complete recovery from the mini-crisis that hit in the spring and summer of 2017. Internal issues at alternative lender **Home Capital Group**, which just barely avoided collapse, sparked a bloodbath for housing-connected stocks and led to policy changes initiated by the Ontario provincial government.

Positive signs in the market include a forecast median price gain between 1.5% and 2% for 2018 from **Reuters** analysts. This same report projects prices to increase 2% in 2019 and 2.1% in 2019. This is muted in comparison to market conditions Canadians have experienced over the past several years, but policymakers will be pleased with the forecasted stability.

Moody's Analytics has also predicted stability in the Canadian housing market going forward. Swiss bank UBS, however, has listed Toronto and Vancouver among the top five in its Global Real Estate Bubble Index. Both come in behind Hong Kong, which took the top spot, and Munich. Toronto was down from a first-place ranking in 2017.

Alternative lender stocks have been relatively calm over the past several months, ignoring the most recent global stock market sell-off. However, the company we will look at today has seen its stock plummet sharply over the past month. Could it be the canary in the coal mine for Canada housing? Let's dive in.

MCAN Mortgage (TSX:MKP) is a Toronto-based mortgage investment company. It aims to generate income by investing in a portfolio of mortgages that include single family residential, residential construction, non-residential construction, and commercial loans in addition to other types of investments linked to loans and real estate. Shares have dropped 30.2% over the past month as of close on October 23.

MCAN released its second-quarter results back on August 9. Total mortgage arrears grew to $21 million at June 30, 2018, compared to $19 million at March 31, 2018. That balance consisted entirely of single-family mortgages, $3.8 million of which were uninsured.

MCAN added that the new OSFI mortgage rules instituted in January have impacted approximately 10-15% of the mortgages underwritten at the company. It also pointed to uncertain conditions in the broader real estate market as being a source of concern for generating growth in mortgages going forward. The company has elected to re-position itself during this period and will focus more on single family mortgages. There are significant challenges in realizing growth in the current market, as the company emphasized in the last quarterly report.

A summer report from Mortgage Professionals Canada stated that over 100,000 Canadians had been prevented from buying homes due to the new stress test for uninsured buyers. The report also said that re-sale activity had dropped 12.5% year over year and reported that home ownership had fallen to 67.8% compared to 69% in 2011.

MCAN dropped its quarterly dividend by $0.05 per share to $0.32 on September 24. This still represents a monster yield of 11%, but income investors have better options considering the performance of the stock. This month the company announced that its chief financial officer Jeff Bouganim would resign from the company effective November 26, 2018.

The struggles at MCAN do not portend reckoning for the Canadian housing market, but its struggles illustrate a sharp change for the industry. Soaring valuations and ballooning mortgage loan growth will no longer go hand in hand, especially as the supply crunch is projected to worsen. This is bad news for MCAN, but a period of cooling may be healthy for Canada housing.

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