3 Reasons Canada Housing Looks Strong Heading Into 2019

Description

The state of the Canadian housing market has been a source of anxiety for investors and policymakers alike since early 2017. The housing bubble reached its peak in Ontario in the spring of 2017, and the province followed suit by introducing new regulations to cool the market. So far, these regulations have been a success. Alternative lender stocks, which were pulverized in mid-2017, have since bounced back nicely.

Today we'll look at three reasons the housing market is carrying renewed strength heading into 2019. We will also review alternative lender stocks that should benefit from this improved environment.

Stabilization of the market

The rate of home sales dropped sharply in the months following the introduction of a foreign buyer tax in Ontario. The OSFI introduced a stress test for uninsured buyers that took effect in January 2018, which also had a negative impact on year-over-year sales. Home prices fell sharply from highs in the spring of 2017, but have since stabilized and are up approximately 2% year-over-year across Canada.

Prices are expected to report modest gains in 2019 and 2020, while home sales have reverted to the 10-year average in recent months. These indications point to a balanced market, which is cause for celebration heading into the new year.

Real estate investment looking attractive again

The year-to-date increase in home prices looks better when reflecting on the state of the stock market in late November. The **S&P/TSX Composite Index** had dropped 7% in 2018 as of early afternoon trading on November 22. Earlier this month I'd discussed how we have arrived at a "lost decade" for the TSX index and what this could mean going forward. The Canadian real estate sector has been one of the few sure bets over this period, which has again been the case in 2018.

Alternative lender stocks have been a surprise bright spot in late 2018. **Home Capital Group** (TSX:HCG) had surged 27% month-over-month as of early afternoon, trading on November 22. Net income rose 10.1% quarter-over-quarter to $32.6 million, or $0.41 per share. Mortgage originations also grew to $1.44 billion, up 16.7% from originations in the second quarter and over 270% year over year.

Home Capital is in a great position in terms of liquidity heading into 2019. The company has bounced back nicely from the brink and new regulations have boosted retention rates. However, as it stands, Home Capital looks overbought at an RSI above 70, so investors may want to wait for a pullback before jumping in.

High immigration levels will continue to drive demand

The high rate of immigration into Canada is projected to keep demand high into the next decade, especially in major metropolitan areas. Housing affordability will continue to be an issue that policymakers wrestle with, but this factor will contribute to keeping sales balanced while also providing support to home prices. There is no indication that supply will come close to catching up to this demand in the years to come.

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