Is a Housing Market Crash Likely in 2020?

Description

As the COVID-19 shutdown persists, Canada's real estate sector enters a deep freeze. With millions of people unemployed, small businesses on the brink, and mortgage lending tightening, could this be the start of a housing market crash? If so, should investors sell their residential real estate investment trusts (REITs)?

Triggers of a housing market crash

A sudden decline in median income and a pullback in credit could be the triggers that toppled Canada's housing market. With the ongoing shutdown, millions of Canadian have unfortunately lost their jobs. It may be fair to say the country's ability to afford a home has declined.

Meanwhile, the failure of individuals and businesses to service their debt could trigger a credit crisis. Banks could tighten lending rules, which could further limit the buyers' purchasing power.

In the end, a combination of tougher lending and spiking unemployment could compel homeowners to sell their properties for less. However, this pullback in prices is far from a crash and could be temporary.

Reasons for optimism

The fundamentals of the residential real estate market in major Canadian cities remains optimistic. Immigration could resume once the shutdown is over and the viral outbreak is tamed. Professionals who can work from home could sustain their income, despite the downturn. The economy is expected to bounce back, even if it takes a few years.

Meanwhile, the federal government has stepped in to support Canadian households. A wage subsidy and various economic concessions could put a floor on the economy and prevent a housing market crash. These measures could prevent plenty of economic distress across the country.

Opportunities

Investors who expect a near-term pullback followed by a long-term recovery could see an opportunity to invest in REITs.

Canadian Apartment Properties REIT (CAPREIT), one of the largest residential REITs in the country, offers a 3.3% dividend yield. The stock has declined 31.8% over the past month and is currently trading 19.5 times net funds from operations per share.

CAPREIT's peers, **Minto Apartment REIT** and **Killam Apartment REIT**, have faced similar declines in recent months. Since the stock price has declined, these REITs are offering better dividend yields.

However, investors need to tread carefully. Avoid REITs with too much leverage, exposure to regions with unique economic problems (Alberta) or lacklustre credit ratings. Cash is king, so focus on trusts with enough liquidity.

Bottom line

These are unprecedented times. We've never seen unemployment and business failure on this scale before. Unfortunately, it seems like the ongoing pandemic could leave a permanent imprint on our economy and lives.

This chaos could extend to the residential property market later this year. However, there is reason to believe Canadian homes could retain their value, and households will be supported by the government's fiscal efforts. This could make residential real estate a lucrative bet.

For investors with a stomach for inordinate risks, the residential property market could be ripe for a contrarian bet. Take a closer look and pick trusts with robust balance sheets and good credit.

Good luck and stay safe!

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