Will COVID-19 Lead to a Housing Market Crash in Canada?

Description

The COVID-19 pandemic continues to wreak havoc on a global scale. The deadly virus has now affected 1.85 million people and resulted in close to 115,000 deaths as of April 12, 2020. Canada reported over 24,000 cases with 16,494 cases still active at the time of writing.

The COVID-19 has led governments to announce countrywide lockdowns resulting in shutting down of businesses, schools and colleges. There has been a significant decline in consumer spending as people are just buying the essentials such as groceries and medicines. The closure of businesses will result in high unemployment rates, which may trigger a housing market crash in Canada.

Individuals will find it hard to service their debt in these uncertain times driving default rates higher. The Canadian banks may be compelled to tighten lending, which again would result in a lower number of mortgages.

Is COVID-19 a near-term headwind?

The COVID-19 first originated in China. The Asian giant is now reopening businesses and airports after a 76-day lockdown in Wuhan, the epicentre of this virus. While China is slowly limping back to normalcy, we can expect other regions to soon follow suit, making the current situation a temporary headwind.

Canada will continue to experience an influx of immigrants once borders are reopened, which will help sustain housing demand in major markets of Toronto and Vancouver. These two large cities have experienced a massive surge in demand for obvious reasons, resulting in a staggering rise in property prices.

While the COVID-19 issues may be resolved in the next few months, its after-effects may linger for a long time. Several economists have predicted a recession far worse than the financial crisis of 2008-09.

A low interest rate environment will be offset by a spike in unemployment rates and a delayed market recovery. The high debt-to-income ratio of Canadians may just spell doom for the country’s housing markets.

We can see here that almost 500,000 Canadians have applied for mortgage deferrals since the shutdown began — a number that will likely to move higher in the coming weeks.

The Canadian government has pumped in over $100 billion dollars into the economy to help businesses, individuals and families. However, this might not be enough to boost the economy given the long-term impacts of the COVID-19.

What next for investors?

REITs are popular for several reasons. They give investors real estate exposure without having to take on a significant amount of debt. REITs provide generous dividends due to a stable stream of cash flows and can grow their portfolio via acquisitions.

But what if recession fears come true and Canadians find themselves in the midst of a housing crash by the end of 2020? Is it then time to exit real estate investment trusts (REITs) with high leverage ratios and consider buying diversified stocks in this sector like **Morguard REIT**?

Will banks such as **Canadian Imperial Bank of Commerce** and **Royal Bank of Canada,** with high exposure to the housing market see a further decline in stock prices?

Amid a highly volatile environment, investors can look to park their funds in REITs with a diversified portfolio, low debt and low payouts. **CAP REIT** is one such REIT with a long-term debt to equity ratio of 60% and a payout ratio of just 18.2%, lower than the overall industry standards, which will help the company maintain its dividend yield of 3%.

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