Will the Canadian Housing Market Crash in 2020?

Description

The coronavirus (COVID-19) isn't the only thing that could trigger a brutal Canadian housing market crash this year. The sudden collapse in oil prices as a result of the coronavirus-induced demand shock has severely exacerbated the unprecedented rise in unemployment from coast to coast.

Such a one-two punch could very well trigger the Canadian housing market crash that some have been talking about over the past few years.

Credit is now hard to come by, the national unemployment rate is skyrocketing, the Canada Emergency Response Benefit (CERB) may not be enough, and mortgage deferrals may prove to be a temporary response that only serves to delay the inevitable Canadian housing market crash.

If furloughed employees aren't rehired over the near- to intermediate-term, we could see another wave of mortgage defaults like during those witnessed in the 2007-08 Financial Crisis.

Real estate investment trusts (REITs) have taken a brunt of the damage amid the coronavirus downturn (some retail and office REITs lost well over half of their value).

And if that's any indication of what's to come for the Canadian housing market, investors should seek to limit their exposure to uninsured mortgages should they be next in line to sour.

Canadian housing market crash: A growing possibility amid the coronavirus pandemic

You can only defer mortgages for so long.

I see mortgage deferrals as akin to the teaser rate period in the lead-up to the Financial Crisis. Although there's no foul play this time around, the mortgage deferral period, like teaser rate periods prior to 2008, do *not* make for a sustainable payment plan over the long haul.

They both assume that the income of the mortgagor will be at a level to meet payments after the expiry of each respective period — an assumption that may not be safe to make.

There *is* still hope for the housing market should a return to normalcy be in the cards this year. But the longer the pandemic drags on, the higher the odds that a Canadian housing market crash will occur.

If deferrals continue dragging and employment never recovers to pre-pandemic levels, I wouldn't at all be surprised to hear default as the "d" word that follows deferrals.

That's the real risk that comes with being a mortgagor. Only time will tell whether the Canadian housing market is going to crumble as it did just over 12 years ago, but if you're not of the belief that we're in for a V- or U-shaped economic recovery, it may be wise to steer clear of stocks with a large number of uninsured mortgages like **CIBC**, the bank viewed as the most vulnerable to a Canadian housing crash.

Many pundits were previously in the belief that the hot Canadian housing market would cool off gradually rather than implode violently. But you need to remember that none of these folks foresaw a pandemic nor the catastrophic implosion in oil prices.

Who knows what these same pundits see happening now?

The odds of a Canadian housing market crash seem to be increasing

I urge investors not to entirely rule out the possibility of a housing market crash happening within the next two years, especially if the recent bout of job losses are not as temporary as they seem and the pandemic continues to take a toll on the global economy.

I'm an optimist, however. And I do think we're in for a V- or U-shaped economic recovery once the risk of contracting COVID-19 is lowered drastically. A majority of mortgage payments could very well be back on their regular schedule as soon as a few months, and a disaster could be averted.

However, there's always a chance that the economy could be crippled for a longer duration should a second wave of the coronavirus spark another lockdown, devastating the incomes of Canadians for a longer duration.

As nice as it is to be an optimist through these dark times, you must weigh the risk/reward and *always* consider the bear case — a Canadian housing market crash.

Foolish takeaway

With all the uncertainty regarding the coronavirus, I'd argue that the bear case is detrimental, and one should seek to limit their exposure to the insured mortgages if they can help it.

The problem isn't about the credit quality this time around; it's an unforeseen health disaster that could spread to even the prime mortgages.

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