Will Canada's Housing Market Collapse in 2020?

Description

Lately, there has been a lot of speculation as to the state of Canada's housing market in 2020. With COVID-19 hitting the economy where it hurts, it's hard to think there will be no effect.

However, the actual data so far has been ambiguous. Recently, the Real Estate Board of Greater Vancouver reported that the city's real estate prices actually rose 2.5% in April. The report indicated a slowdown in sales but not a reduction in cost. We're seeing similar reports from Toronto, whose housing market has cooled without getting more affordable.

These early indications would tend to suggest that the housing market is not collapsing. But is this an indicator of what's to come or merely the calm before the storm?

What economists are saying

Since the COVID-19 lockdowns began, we've had a number of economists chime in on the future of Canadian housing.

Benjamin Tal and Katherine Judge of **CIBC** said weaker fundamentals would result in "downward pressure on prices."

Rishi Sondhi of **TD** said that Toronto home prices would rise 8% in 2020, while affordability would decline.

Moody's Analytics, however, forecast a 30% drop in prices.

Overall, the commentary from experts has been mixed. Almost all economists agree that sales volume will slow in 2020, but there is no consensus on whether that will hit prices. Regardless of what happens, though, there's one real estate industry that's almost certain to suffer this year: REITs.

REITs could run into trouble

REITs could run into serious trouble in 2020 regardless of what happens to the housing market. The reason is that they depend on rental income, which is under serious pressure right now. It goes without saying that out-of-work Canadians will have trouble paying rent.

The bigger story is the potential for default on commercial leases. Recently, the U.S. company **Cheesecake Factory** said it wouldn't be paying its landlords in April. Citing a lack of cash, management said they just couldn't afford to.

That's a bad sign for REITs like **RioCan Real Estate Investment Trust** (TSX:REI.UN).

RioCan invests in retail and residential space — two real estate sectors that are getting hit right now. Retail space is under pressure from forced business closures, while residential space is under pressure from rent deferrals.

On Tuesday, RioCan released its first-quarter earnings press release. It had a brief section on the effects of COVID-19, but it was fairly vague. One clue it did provide was that it suspended its same-property NOI guidance. This indicates that the company doesn't expect to hit its previous performance targets. The company did manage to grow its funds from operations (FFO) slightly in Q1. However, per-unit FFO declined from $0.47 to $0.46.

We'll still have to wait and see whether RioCan will suffer from a wave of delinquencies. So far, it looks like it's holding up all right. But already we're beginning to see certain U.S. REITs feel the heat. There's no reason that Canadian REITs couldn't suffer the same fate.

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