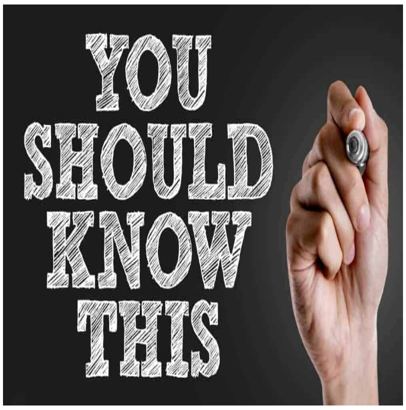

Housing Market Crash: CMHC Says Canadian Home Prices May Fall Up to 18%!

Description

Ever since the COVID-19 lockdowns started, a lingering question has been the pandemic's effect on housing prices. Early on, we saw sales decline in most cities, but that didn't translate into lower prices. At the same time, many experts forecast that fewer sales would translate to lower prices eventually.

Analysts at **Scotiabank** and **CIBC** forecast price declines, while other analysts anticipated continued gains. Overall, there was a wide range of opinions, and no clear consensus.

Recently, the Canada Mortgage and Housing Corporation (CMHC) jumped into the fray. In a report dated May 27, it forecast a 51-75% decline in housing starts, a 19-29% drop in existing home sales, and a 9-18% drop in house prices. That latter figure is the most significant. So far, slower housing sales haven't translated into lower prices. Now, the CMCH is saying that they will.

When the nation's largest housing organization speaks, industry participants listen. In this case, the response has been largely negative, with RE/MAX slamming the CMHC's report as "panic inducing*."* Whether you agree with that or not, the forecasts the CMHC put out are worth listening to as they shed light on the state of the housing market in 2020.

Factors at play

The two big factors that contributed to the CMHC's bearish forecast were high unemployment and low immigration. In the COVID-19 era, millions of jobs were lost as businesses shut down to comply with lockdown orders. Simultaneously, immigration fell as Canada closed its doors to international travel.

We'd expect that both of these figures to lead to lower housing prices. Fewer jobs means fewer people who can afford to buy houses. Fewer immigrants means less population growth–another key driver of housing demand. With these two developments occurring simultaneously, you'd expect house prices to fall. This reasoning seems to have been the basis for the CMHC's bearish forecasts.

Implications for investors

Before getting into the implications of the CMHC's report for investors, one thing should be emphasized:

Economic forecasts aren't infallible. Even when you've got a huge budget and access to piles of industry data, you can still get it wrong. But the CMHC does have many of the country's foremost experts on housing, so its opinions should be taken seriously. With that in mind, here are some implications for investors should the CMHC's forecasts prove correct.

First, real estate investments will perform poorly this year. Despite the fact that house price declines are expected, they haven't materialized yet. On May 15, the CBC reported that home prices were flat despite a 56% drop in sales, suggesting that price declines are coming at some point in the future. If you think that the CMHC's forecast is correct, now isn't a good time to buy.

Second, REITs are probably in for some trouble– particularly REITs with residential investments like **RioCan Real Estate Investment Trust** (TSX:REI.UN). While RioCan doesn't buy and sell houses, the same factors that will hit single family homes, will hit apartments.

When more people are out of work, more people default on their rent. With less immigration, there's less demand for housing. So we'd expect REITs to suffer in this environment.

If you look at RioCan, for example, it owns a mix of commercial and residential properties. Many of its buildings have big box stores on the bottom, with residential units above. In the first quarter, RioCan saw a $2.4 million decrease in operating income from residential rentals.

That doesn't appear to have been due to increased defaults or lower demand, but shows that the company is vulnerable to these factors should they materialize. So far, we're not seeing any major damage. But if the CMHC is right, it could be coming.

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Date
2025/08/24
Date Created
2020/06/09
Author
andrewbutton