Housing Bubble: Protect Yourself From a Real Estate Implosion

Description

There's a housing bubble in Canada. House prices remained stable throughout last year and are now surging to all-time highs. Meanwhile, household income and rent remains suppressed. This disconnect between earnings and price is a clear indicator of a bubble. And like all bubbles, the housing bubble could be at risk of popping.

If you're an investor, particularly one with exposure to real estate, here's what you need to know.

Drivers of the housing bubble

Potential home buyers across Canada have been patiently waiting for house prices to become more reasonable. Last year could have offered buyers an opportunity to enter the market, but sellers delisted their homes. Meanwhile, the government suspended mortgage payments and lowered interest rates to make mortgages historically cheap.

Now, with the crisis receding, pent-up demand and cheap capital are pushing prices higher. That's creating a clear housing bubble. Some experts have even compared what's happening in Canada now to what happened in the U.S. during 2005 to 2007.

Is a pop inevitable?

The key driver of house prices seems to be interest rates. If mortgages become more expensive, buyers will be priced-out causing the housing bubble to pop. However, the government remains committed to keeping interest rates low.

In fact, the Bank of Canada has officially said interest rates could remain at current levels until 2023. That means capital could remain cheap for several years, inflating the housing bubble further.

However, if the inflation rate picks up faster than the BoC expects, they could be compelled to raise rates sooner. This could potentially pop the housing bubble.

Protect yourself

Rising inflation and falling house prices would be great for home buyers, but detrimental to the economy. Real estate is the largest component of Canada's economy, by far.

Investors who expect a pop may want to limit their exposure by cutting stakes in banks, real estate investment trusts and credit firms. Instead, protecting against inflation could be a better bet.

Gold is traditionally seen as an inflation-hedge. Adding **Barrick Gold** to your portfolio could be one way to mitigate the risk of inflation. You could also add defensive stocks such as **NorthWest Healthcare REIT** to your portfolio. The company's leases are locked-in for several years. The average age of its contract is roughly 14 years — couple that with the fact that healthcare services are disconnected to the rest of the economy.

Defensive and commodity stocks tend to do better when there's panic and inflation. These stocks may provide a buffer when things get rough. They could also be excellent bets if the housing bubble pops.

Bottom line

Canada's undoubtedly experiencing a housing bubble. House prices have climbed to record-highs, even as rent and income have dropped. The government sees this as a side-effect of protecting the economy with added stimulus. But if inflation picks up faster than expected, the government could be forced to raise rates causing the housing bubble to pop.

If you're concerned about this, adding gold or a defensive healthcare stock your portfolio could be the best bet. Good luck!

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