



UBS Report: Canada Has the 2nd-Biggest Property Bubble in the World

Description

The Bank of Canada is on guard regarding the country's housing market. Deputy Governor Lawrence Schembri has said before that house prices had increased relatively rapidly in recent months. UBS noted that falling mortgage rates reignited price growth.

The global Swiss bank's annual Global Real Estate Bubble Index shows that Toronto (second) and Vancouver (sixth) are among the top 10 major cities in the world with high bubble-risk scores. UBS noted the irrational exuberance in Canada, and the trend is accelerating much faster compared with other countries.

Bubble on a bubble

Canada's real estate bubble could be a bubble on a bubble based on the U.S. Federal Reserve's Exuberance Index for Q1 2021. The said index measures buyer enthusiasm for higher prices. It also measures the prices paid in contrast with fundamentals. According to the Feds, it could result in a correction at some point, although they can't say when.

Meanwhile, real estate investors should be mindful of speculative activities that tend to inflate prices. But if you fear the bubble bursting, real estate investment trusts (REITs) are the next-best alternatives. Besides less capital outlay, Canada's top REITs pay [dividends](#). It's like receiving rental income without owning physical properties.

Growth-oriented

Killam Apartment ([TSX:KMP.UN](#)), a \$2.45 billion [growth-oriented](#) REIT, owns, operates, and develops apartments and manufactured home communities (MHCs). Thus far, in 2021, its rental business is doing great. In the first half of 2021, property revenue, net operating income (NOI), and net income grew 7.4%, 7.2%, and 173.4% compared to the same period in 2020.

Management admits that Killam benefits from the low-interest-rate environment, particularly on

mortgage refinancing. Moreover, lower interest rates contribute to earnings growth. Notably, the strong occupancy (96.9%) compensates for the government-imposed rental rate freeze.

Killam trades at \$23.02 per share and pays a decent 3.04%. The REIT is also a steady performer on the TSX with its 37.73% year-to-date gain. Management expects the rent freeze to be over in 2022. Since Killam is also student-focused, demand for rental units should rise when in-person classes begin.

Dividend and recovery play

RioCan ([TSX:REI.UN](#)) is one of the largest Canadian REITs. This \$7.2 billion REIT is retail-focused and boasts high-profile tenants such as **Loblaw**, **Metro**, and **Canadian Tire**. RioCan Living, the residential brand, was launched in 2018 and is now cultivating opportunities to convert select existing retail shopping centres into mixed-use communities.

In the first half of 2021, RioCan reported \$252 million in net income versus the \$247.9 million net loss in the same period in 2020. According to Jonathan Gitlin, its president and CEO, the quarterly results demonstrate strength and recovery momentum.

With the ongoing momentum in leasing activity, RioCan is an excellent dividend and [recovery play](#). Performance-wise, the stock is up 39.53% year to date. At \$22.57 per share, the dividend yield is a lucrative 4.25%.

Abrupt end of the housing frenzy

UBS believes the housing growth will end soon saying, "The Bank of Canada is expected to taper in 2022, well ahead of the Federal Reserve." It can't allow the low-interest-rate environment to continue, because it might create a giant bubble.

The Swiss bank, however, added that such a move would likely raise mortgage rates. It could also discourage foreign real estate investments. Both could abruptly end the current housing frenzy.

CATEGORY

1. Dividend Stocks
2. Investing

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