Multiple Rate Hikes in 2022 Spell Trouble for Homebuyers

Description

The typical peak of housing activities in Canada is coming in spring. Many homebuyers look to forward to the home-buying season, hoping there's more inventory and no bidding wars. Unfortunately, it could still be a sellers' market by then, despite efforts by the Bank of Canada to cool the red-hot sector through rate hikes.

A temporary price drop is more likely than a significant correction in home prices. Meanwhile, homebuyers would be at a disadvantage if the central bank implements more rate increases until year-end. Besides inflated prices, multiple rate hikes spell trouble for them.

The shock waves

The federal government is under pressure to solve the prevailing housing affordability crisis and bring back the market balance. Two of the proposed measures to lessen competition is a ban on foreign ownership and an anti-flipping rule. There's also a $4 billion budget to double home construction in five years.

The focus on the real estate industry is commendable, although continuous rate hikes would increase financing costs or cut the purchasing power of homebuyers. Sung Lee, a mortgage agent at RatesDotCA, said, "Higher and faster rate hikes will affect mortgage affordability for a significant population of homebuyers."

Capital Economics analyst Stephen Brown added, "There simply may not be enough people who can afford the current prices at a higher cost of financing." Toronto-based mortgage broker Reza Sabour confirmed the 10% drop in the purchasing power of buyers over the past months. He said, "There's definitely going to be shock waves if rates continue like this."

Investment options

The Trudeau administration has plans to weed out real estate investors that make up made one-fifth of the housing market with an anti-flipping measure. A full taxation on profits or business income looms on any person who sells a residential property held for fewer than 12 months. However, there could be exemptions depending on certain life circumstances.

For real estate investors looking to earn rental-like income without owning physical properties, a real estate investment trust (REIT) is the route. REITs trade like dividend stocks and are great sources of passive income. **Nexus** (TSX:NXR.UN) and **Summit Industrial** (TSX:SMU.UN) in the industrial sub-sector are the best choices. Both REITs benefit from the e-commerce boom and pay attractive dividends.

Nexus is a standout today. Besides the 62.97% trailing one-year price return, the dividend yield is a generous 4.90%. At $13.05 per share, the stock price of this $1.03 billion pure-play industrial REIT is a steal. Because of a strong start this year, management is hopeful that 2022 will be equally successful as 2021.

Summit Industrial owns and operates light industrial properties. At $20.21 per share, the dividend yield is a decent 2.7%. For 2022 and beyond, this $4.04 billion REIT will continue to expand its development pipeline. Its recent joint venture partnership aims to create a central shipping and logistics hub to service southwest Ontario and the GTA plus clients near U.S. border crossings.

Near-term goal

While Mr. Brown isn't against interest rate hikes, he hopes that home prices drop to what a median household can afford. According to BoC governor Tiff Macklem, the central bank may need to take rates modestly above neutral for a period. It should bring demand and supply back into balance and inflation back to target.

CATEGORY

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Date
2025/09/18
Date Created
2022/04/20
Author
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