Mid-Year Shock: A 0.75-1% Rate Hike Is Next

Description

Economists were taken aback by the 6.7% inflation reading in March 2022. Based on data from Statistics Canada, the rate is a 31-year high. Moreover, prices in all eight categories of Canada's economy like food, energy, and shelter spiked. Royce Mendes, an economist at Desjardins Group, confirmed that the jump in prices last month was the largest since January 1991.

With the cost of living this high, the 50-basis-point increase in interest rate on the 13th of April could be a prelude to a one-shot, goliath rate hike. For Derek Holt, Head of Capital Markets at **Scotiabank**, the situation justifies a 0.75-1% rate hike by the Bank of Canada come mid-year when the policymakers meet again.

Mortgage affordability

Homebuyers would be doubly concerned if the surge in inflation prompts the central bank to raise its key interest rate to 1.75% or 2%. While multiple rate hikes can bring down home prices, it would impact mortgage affordability. Leah Zlatkin, a licensed mortgage broker at LowestRates.ca., warns of a roller-coaster experience for current and prospective homeowners if rates keep going up this year and the next.

The Canadian Real Estate Association (CREA) reports that the real estate market slowed down in March, although it doesn't see bargains anytime soon. Despite sales dipping 5.4% month over month, activity remains historically high, and home prices rose 27.1% year over year.

Shaun Cathcart, CREA's senior economist, says moderating prices is a good thing, but the opposite could happen. He thinks that raising interest rates in the near term to cool the housing market won't help affordability. Cathcart added that the $4 billion budget by the federal government to accelerate home construction is a long-term solution.

Invest in REITs

The federal government will introduce anti-flipping measures and a two-year ban on foreign ownership to lessen competition among local homebuyers. For real estate investors, there's a route to earning rental-like income without direct ownership. Instead of purchasing physical properties, invest in real estate investment trusts (REITs).

A valued and prominent passive-income provider today is **Granite** (TSX:GRT.UN). This $6.37 billion REIT owns and manages in demand logistics, warehouse, and industrial properties in North America and Europe. Furthermore, Granite is a Dividend Aristocrat whose dividend-growth streak is 11 consecutive years.

Performance-wise, the REIT's total return in 3.01 years is a decent 80.09% (21.6% CAGR). If you invest today at $100.40 per share, the dividend yield is 3.11%. Besides the safe payouts, expect growing income for years to come.

Anxiety for homebuyers

Oxford Economics said that home prices in late 2021 were 19% above the borrowing capacity of median-income households. Unfortunately for homebuyers, Oxford expects it to rise 38% above what the average household can afford by the mid-2022. Meanwhile, it forecasts home prices to decline 24% by mid-2024.

For Tony Stillo, director of Canada Economics at Oxford, the triggers for a downward spiral of lower house prices are house prices themselves. He said the housing market could reach a breaking point and crash under the weight of its own success before year-end 2024.

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