Notice to Buyers: Home Prices Could Drop 15% by Year-End 2023

Description

Rising interest rates will slow down activities in Canada's red-hot housing market, although homebuyers can't expect a price relief yet. The earliest it could happen could be 18 months from now. Desjardins's senior director of Canadian Economics Randall Bartlett and senior economist Helene Begin said prices could "plausibly" fall 15% by the year-end 2023

The Canadian Real Estate Association (CREA) reports that home prices have fallen sequentially for the last two months from a non-seasonally adjusted record of $816,720 in February 2022. Many industry experts believe that the aggressive rate-hike campaign by the Bank of Canada to combat inflation is starting to weigh on the housing market. Homebuyers are also rethinking their options.

A correction to bring back balanced conditions

Desjardins's economists are certain that despite rising interest rates, the Canadian housing market will only bend but not break. They said, "Looking ahead, we believe ever-higher borrowing costs are going to weigh on housing market activity as increasingly interest-sensitive households batten down the hatches for the impending storm."

A sustained weakness in sales activity should lead to persistent downward pressure on prices. The same economists also said that the expected housing market correction has begun, although it's not yet widespread. More importantly, it should help bring back more balanced conditions, contrary to the previous supercharged run.

Impact to homebuyers

Some prospective homebuyers have pulled out or deferred purchases because of rising borrowing costs. John Pasalis, president of real estate brokerage Realosophy, said, "The full impact of the Bank of Canada's interest rate hikes likely won't be felt by homebuyers until the summer months, when many locked-in mortgage rate contracts expire."

Lauren Haw, CEO of Zoocasa, said both buyers and sellers are on stand-by. She said, “The housing market pre-priced this rate hike and most people expected it, but what wasn’t expected was the signal of ongoing uncertainty around what rate decisions will look like in the coming months.”

Investment alternative

For real estate investors, direct ownership isn’t the only option. Real estate investment trusts (REITs) are profitable alternatives. Apart from lower cash outlay and zero landlord responsibilities, REITs pay dividends. The payouts can take the place of rental income. Moreover, the stock price could appreciate.

H&R (TSX:HR.UN) outperforms the TSX year to date at +13.82% versus -2.03%. The $4.1 billion REIT has ownership interests in high-quality office, industrial, residential, and retail properties. At $14.01 per share, the dividend offer is 3.92%. A $30,650 position will generate $100.12 in passive income every month.

In Q1 2022, rentals from investment properties declined 24.3% to $201.7 million versus Q1 2021. However, net income rose 508.2% year over year to $970 million. H&R’s CEO, Tom Hofstedter, said, “Our strong first quarter financial results mark a pivotal moment in the continuation of our transformation and the surfacing of the embedded value within our portfolio.”

Silver lining

The central bank has raised its key interest rate three times already in 2022, and economists believe the next hike in July could be 75 basis points. Still, Pasalis says the situation is a silver lining for first-time homebuyers. Higher interest rates are deterrents for Canadians buying homes or real estate for investment purposes.

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