Housing Affordability Is Out of Reach for Many Canadians

Description

The housing crunch in Canada is on, following four interest rate hikes beginning in March 2022. Bankers and economists believe that the subsequent increase could be 75 basis points after the inflation reading in May jumped to 7.7% from 6.8% in April. Instead of price reliefs, aspiring homeowners will have to contend with higher mortgage payments plus other homeownership-related costs.

Residential tenancy should also rise due to the housing and mortgage affordability crises. Life would also be difficult for renters if landlords squeeze them to raise rental payments. Recent data from **RBC** Economics suggests that it's impossible for many residents, particularly in Vancouver, to carry home costs without obtaining debt.

Worsening housing affordability

The bottom line in the changing real estate market is that homeownership costs have become too steep for many Canadians to afford. Wealth Financial Advisers' founder and principal Elke Rubach said on homeownership, "Most of us want to own something, but you have to understand, at what cost? You don't want to overleverage yourself."

Meanwhile, the Office of the Superintendent of Financial Institutions (OSFI) expressed concern over the finances of Canadians. The aggressive rate hikes will cause a heavy burden. According to the banking regulator, they need to tighten requirements on some types of real estate loans to serve as protection. For lenders, reverse mortgages or loans with shared equity features are risky.

Painful for homeowners

Robert Hogue, RBC's assistant chief economist, said rate hikes would be particularly painful for homeowners in the country's priciest markets. He added, "Affordability to get even uglier in Vancouver, Toronto, and Victoria." RBC's gauge of housing affordability will deteriorate by 8.8% in Vancouver with a one-point rate increase. The national average is 5.5%.

Hogue said mortgage payments, property taxes, and utility bills for a benchmark single-family detached home in Vancouver comprised 111.1% of median pre-tax household income in Q1 2022. It was up 21.9% from a year ago and increased 10% from Q4 2021.

At a national level, RBC said it took 54% of pre-tax household income to cover home ownership costs across all property types in Q1 2022. Hogue described the situation as the worst affordability in about 30 years, which could worsen. In the near term, the Bank of Canada's aggressive rate-hike campaign will inflate ownership costs further.

A practical option for investors

For real estate investors, investing in real estate investment trusts (REITs) instead of direct ownership is the practical option today. **Morguard North American Residential REIT** (TSX:MRG.UN) pays an attractive 4.25% dividend. At $16.20 per share, a $141,500 position will generate $6,013.75 in passive income, or $501.15 every month.

The $912 million REIT owns residential apartment communities in Canada (two provinces) and the U.S. (nine states). Morguard's leasing activities in Q1 2022 were robust compared to Q1 2021. Its net operating income and net income increased 14.8% and 19.8% year over year. The occupancy rates are 96.3% in the U.S. and 93.8% in Canada.

Challenging for Canadians

While inflation is soaring and interest rates are climbing, homeownership will be increasingly challenging for many Canadians, especially first-time buyers. The real estate market is starting to cool, but housing affordability remains a big question mark.

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