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Canadians pin retirement dreams on not-so-safe houses

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By Andrea Hopkins

TORONTO (Reuters) - A long bull run in Canadian house prices and painful memories of the 2009 financial crisis have convinced many Canadians that their retirement dreams are best left at their own doorsteps - a strategy that many financial planners consider risky.

Indeed, more Canadians than ever are relying on appreciation in the value of their homes to pay the bills in their golden years. It's a trend that worries advisers, especially as savings rates decline and more people say they are comfortable carrying debt into retirement.

As the U.S. housing crash so painfully demonstrated, property values can move in both directions - and quickly.

"It's the old adage -- don't put all your eggs in one basket," said Chris Buttigieg, senior manager of wealth planning at the BMO Retirement Institute (BMO.TO).

Buttigieg says retirees may find it difficult to sell their home in a market that's softening or to find somewhere affordable to live after selling out. And it's just risky to assume a single illiquid asset will fund what may be 30 years of retirement.

Pointing to a 2012 study he authored, Buttigieg said 41 percent of Canadians now consider equity in their home an option to save for retirement and 47 percent said it is their biggest financial asset.

While advisers may question the strategy - which after all eats into their sales of investment alternatives - its popularity is easy to understand.

Urban housing has experienced a long boom in Canada, with prices doubling or tripling in recent decades even as stock market portfolios slumped in the 2009 crash.

"The last 10 years has definitely not been a very positive climate for financial assets," said Dylan Reece, a member of Advocis, the Financial Advisors Association of Canada, and an associate portfolio manager at Nicola Wealth Management in Vancouver, who supports real estate investment in an otherwise balanced portfolio.

"At the same time, real estate has done extremely well, and therefore it is natural for people to project that will continue, and they capitulate on financial assets and say 'I'm better off putting it all in my home.'"

But John Andrew, director of Queen's University Real Estate Roundtable, said an asset that doubles in value over 10 years isn't quite the winner it may seem.

After crunching numbers for annual returns of the Toronto Stock Exchange and the Canadian housing market over the last few housing cycles, Andrew said the two are in many cases a wash.

From 1981 to 2012, the TSX posted an annual return of 5.45 percent, excluding dividends. The appreciation in Canadian home prices represents a 5.6 percent annual return. Booming cities fared not much better, with a 6.17 percent annual return in Toronto housing and a 6.43 percent annual return in Vancouver.

"You may think prices have gone nuts," especially if a real estate investor is just looking at the booming market from 1997 to 2012, said Andrew. But when a longer cycle is considered, the difference is almost nil, he said.

ILLIQUID ASSET

The benefits of real estate investing are widely accepted in Canada, where home ownership rates approach 70 percent. In an era where household debt is at historically high levels and the discipline to save is scant, paying down the mortgage remains the top priority every month.

"It is a forced savings vehicle, a roof over your head, and a beautiful tax shelter," said Andrew. With financial investments, you are paying capital gains or income tax when you make money or cash out for retirement, while a principal residence draws no tax penalties when you sell.

But a good investment is not the same as a good retirement plan, said Mark Coutts, a certified financial planner with Sun Life Financial Inc (SLF.TO).

"Most people are much more comfortable predicting their retirement age than when they will be ready to downsize," said Coutts, noting the inherent timing problems with selling a home just when a retiree is trying to cut living costs.

"The challenge is that while we like owning a home, it doesn't produce income for us, and you can't sell it in pieces -- it is all or nothing," agreed Reece.

Selling a home to fund retirement also means a retiree may have to pay rent, or high costs in a nursing home, rather than living rent-free in an owned home and hiring help. Some retirees may be happy to move to a smaller property or take on a reverse mortgage, but many may feel forced to sell at a less-than-ideal time.

Given growing evidence that the Canadian housing market is heading for a price correction followed by a plateau that may last for years, that ideal time may be now for the bulge of babyboomers who expect to retire in the next decade.

"For those who find their home to be their most significant retirement asset, I suggest take the current opportunity to downsize, free up the equity, and invest in income-producing investments - bonds, preferred shares, income producing real estate or dividend-producing equities," said Reece.

But while he recommends a diverse portfolio, Reece notes financial advisers and experts with the big Canadian banks have good reason to urge investors to focus less on their homes and more on investing in traditional retirement vehicles such as stocks, bonds and mutual funds.

"The banks have two conflicts of interest. The quicker you pay down your mortgage, the less interest the bank will collect. And then they want you to take that money and invest it, and charge fees and commissions to help you do so. It is an interesting double conundrum of conflict of interest."

(Editing by Frank McGurty and Leslie Gevirtz)