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Why the biggest landlord in Canada's North has seen its stock price tank even as rents go up

Financial reporter Tim Kiladze explains the 'astonishing situation' facing Northview

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Crestview Apartments in Yellowknife in 2021. It's one of many residential properties in the North owned by Northview Canadian High Yield Residential Fund. (Walter Strong/CBC)

It's been a sobering spring for one of the North's major residential landlords.

The Northview Canadian High Yield Residential Fund — a major residential landlord in the North, owning the lion's share of private, multi-unit rental housing in Yellowknife and Iqaluit — has seen its stock drop in value in recent months.

In early March, it was trading at more than $12 per share. Its value went down over the next couple of months before seeing a more dramatic drop in mid-May, to less than $8 per share — a three-year low.

It's since risen (trading at $9.67 on Monday), but it's still significantly lower than it's been for much of the last three years.

So what's going on?

"It's a little bit complicated because it's a lot of moving parts," said Tim Kiladze, a reporter and columnist with The Globe and Mail.

Kiladze spoke to Hilary Bird, host of CBC Radio's *The Trailbreaker* in the N.W.T.

This interview has been edited for length and clarity.

Give us a sense of what's been happening with Northview in the last little while.

I would say it really boils down to the state of the economy and where interest rates are and where they could be going.

And it's tricky because the actual units themselves — the apartments — are in pretty good shape. Like, for a real estate company, being in apartments right now is a good thing. You know, rents are going up because there's a housing shortage — which is not a good thing for Canadians broadly speaking, but if you own the real estate, it's a good thing. So you would think that the stock should be doing well, the company should be doing well.

But the problem is that, just like with a regular house, you have a mortgage. And a lot of their mortgages, speaking generally here, are priced at variable rates — so they move when interest rates go up or down. And lately interest rates have been going up, quite a bit. And that puts a lot of pressure on the company because they have to pay more in mortgage debt. It's kind of that simple.

'Being in apartments right now is a good thing ... So you would think that the stock should be doing well, the company should be doing well,' said Tim Kiladze. (Submitted by Tim Kiladze)

The second leg to this is that, the publicly-traded stock so to speak, has a lot of kind of regular investors, retail investors, me and you, who love yield. And yield is essentially just like a monthly payout that you get for holding the stock.

And for a long time interest rates were really, really low and we kind of called it the era of ultra-low interest rates. That changed, obviously, in the last year or so. And so I think this company, their stock would pay about a 10 per cent yield — so if you own $100 worth of the stock, you get $10 in cash each year. And for a long time 10 per cent seemed really, really good. And so it was a great opportunity.

That's all changed. Now, all of a sudden you have investors saying, well, the risk of then having higher mortgage costs coupled with [the fact] you can get high yield elsewhere in other investments, maybe makes this stock or this company is not really worth owning or holding.

Can you talk about what we've been seeing with the actual trust itself, and with those units?

Some of it is just trading off, because the whole real estate market is traded off, is the best way I can describe it.

Because the real estate companies themselves had really low mortgage costs for so long, they were kind of just printing money. As long as you had strong occupancy, meaning there are people in your unit, you're getting a lot of cash, you paid very little in debt or in mortgage, and therefore you could pay a lot of money out to your unit holders or stockholders.

That calculus is changing and so it's made investors much more jittery. And a very crucial development is that in the last quarter, the company has very clearly said, we may have to reconsider our distribution level or, effectively, what we pay out to our shareholders each month. And so that spooked a lot of people and in Canada, where investors tend to love yield, they can make people kind of run for the hills.

From the beginning of March to mid-May, we saw the trust price drop about 30 per cent. Is that a significant drop?

That's a large drop, yeah. And like I said, it's actually been seen in a lot of real estate.

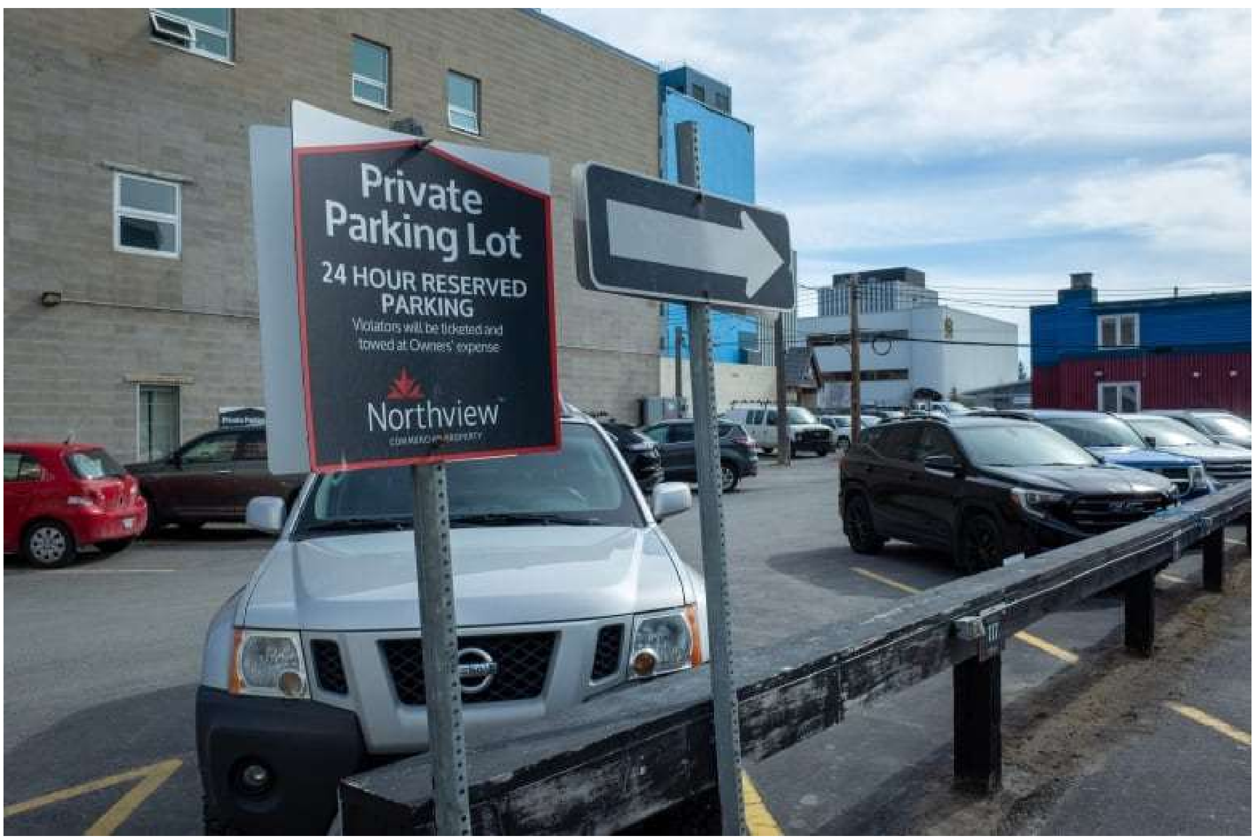
Commercial real estate is kind of divided into sub categories. So you have rental apartments, you have offices, you have industrial properties, a few others. And each one is kind of moving in a different direction right now.

Industrial has actually been really, really strong because we've just changed to kind of of an e-commerce economy or at least we're moving towards them more and more. And so therefore you need more warehouses to store goods close to to major cities.

Offices, meanwhile, are in really bad shape because flexible work patterns and abilities have really made people question how much office space they're going to need going forward.

So those are kind of the two ends of the spectrum. What's strange for Northview is that rental apartments are actually some of the better-performing real estate companies, because there is a housing shortage, we haven't built enough, particularly when it comes to rentals. Occupancy has been quite strong, and there's such tight supply that when a tenant turns over you can see a double-digit rent increase because there's just nowhere else for somebody to go. It's kind of the markets functioning.

But Northview is in that market and performing poorly. And a lot of that has to do with how it's structured, in terms of what its mortgage is or what its debt looks like.



Parking at a Northview property in Yellowknife in 2021. (Walter Strong/CBC)

So essentially what you're saying is that the mortgage, the increase in interest rates, is hurting them a lot more and it's having way more of an impact?

Exactly. So the interest rate effect is outweighing the market dynamics or the increase in rent that they're getting.

Do we know how Northview is faring right now. as a company? Does the stock price, the unit price, sort of reflect how they're doing?

Yeah. So it's very much a reflection of what's going on internally and what investors think about what the company is going to have to do.

A big element of that is, that right now they have positive cash flow, is the best way to describe it. But because interest rate hikes are kind of eating up so much, or interest costs are eating up so much of their cash or cash flow, they're going to have to make some changes.

The change is likely to come on the investment side rather than the actual day-to-day operations of the company. And the change will be the distribution cut. It seems as though they're at least pondering that. Because if you cut that by 50 per cent, you're paying out 50 per cent less each month and that cash can go to helping to pay down your debt.

But there is an element that could affect the company. I don't want to, you know, speak out of school here, because I don't know the exact kind of variables around what their capital expenditures look like, but generally speaking, rental apartments, a lot of the buildings that are owned by publicly-traded companies, are older stock. They're older buildings maybe built in the '60s, '70s, when we had this huge boom of rental housing development in Canada, and they just need upkeep. And for a long time they weren't getting that upkeep, and therefore, you know, lobbies need to be redone, windows need to be replaced. You know, all the things that are actually pretty generic, but it takes a lot of time and a lot of capital, a lot of money. And so if they're really short on money, it means that the building could be left to kind of dwindle for a longer period of time.

Do we know how long that could last?

I don't think anybody knows right now, to be honest.

But with the news that economic growth was much stronger than anybody expected, we might have to raise rates even more and that will put even more hardship on the company in terms of interest cost and its debt. And there's the possibility things get so out of whack that we actually have to jack up rates so much that we actually trigger a recession. Then rates would fall, and they would kind of all reverse. But the timelines — even the Bank of Canada governor doesn't know right now.

What do you think the future looks like for Northview?

To be honest, it's a bit of an astonishing situation because the fundamentals are actually quite strong. You know, there is strong occupancy. We do have a housing shortage. You know, when they set this thing up and and bought a bunch of properties and listed it on the stock exchange, the case all made sense.

What's changed is more of the investment side of things — the investment thesis, is how I would describe it. Because rates have changed so quickly. I think we now know that that era of ultra-low rates is over and it's all about managing and changing expectations for what this new era looks like.

Do you see Northview cutting their distribution to investors in the near future?

I'm not qualified or accredited to give investment advice. I have to be careful what I say. But given where the financials are going and what I've seen, what we've all seen other real estate companies do, it's certainly a possibility.