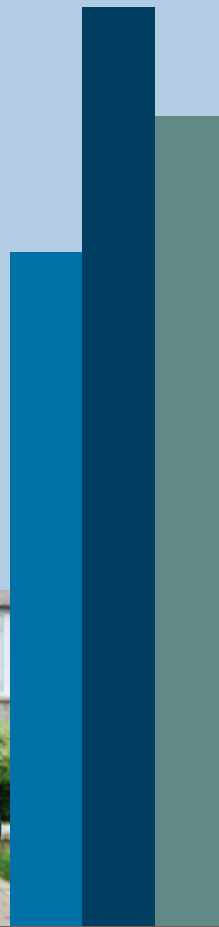


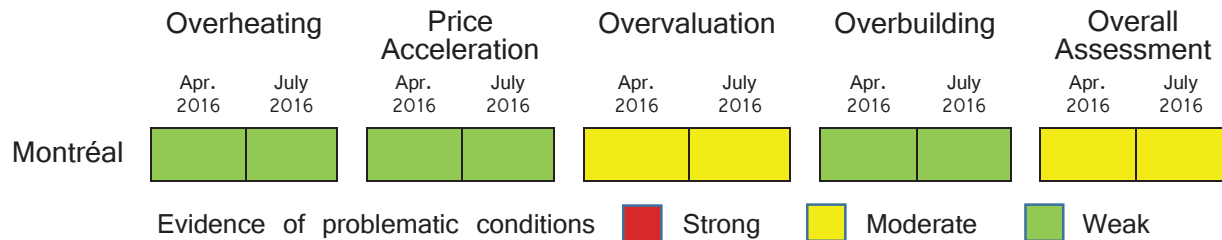
HOUSING MARKET ASSESSMENT Montréal CMA

Date Released: Third Quarter 2016



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Highlights



- The Housing Market Assessment (HMA) analytical framework continued to detect moderate evidence of problematic conditions on the Montréal census metropolitan area (CMA) market in the first quarter of 2016.¹
- Evidence of overheating and acceleration in the growth of prices stayed weak, because supply remained rather high relative to demand.
- Moderate evidence of overvaluation continued to be detected, since the level of prices remained above what would have been expected based on the fundamentals.
- Evidence of overbuilding stayed weak, as the rental housing vacancy rate and the inventory of completed and unsold units per 10,000 population stayed below their respective problematic thresholds.
- The HMA analytical framework considers four factors to assess the evidence of problematic housing market conditions: overheating; acceleration in the growth of house prices; overvaluation; and overbuilding.

HMA Overview²

As Canada's authority on housing, CMHC contributes to market stability by providing information on potential imbalances that could affect housing markets. With the Housing Market Assessment (HMA), CMHC offers information and analysis that can help Canadians make more informed decisions.

The HMA combines the results from a technical framework with insights gained through CMHC's market analysts' knowledge of local market conditions. These insights position CMHC to provide additional context and interpretation to the results of the HMA framework.

The HMA framework detects problematic market conditions in local housing markets by identifying imbalances. An example would be the detection of overbuilding, a situation in which the inventory of unsold new homes accumulates on account of supply outpacing demand. Such an imbalance could be resolved by an adjustment in house prices. As an example, lower prices would help resolve an excess supply imbalance by supporting stronger demand and/or reducing supply. However, other unexpected developments that do not originate from the housing market could accentuate or reduce an imbalance.

Colour codes indicate the level of evidence of problematic conditions. The HMA is a comprehensive framework that considers the intensity of signals of imbalances (that is, how far the indicator is from its historical average) and the persistence over time. Generally, low intensity and persistence are associated with potential weaker evidence of problematic conditions. As the number of intense and persistent signals increases, the associated evidence of problematic conditions becomes stronger.

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¹ Results are based on data as of the end of March 2016 and local market intelligence up to end of June 2016. CMHC continuously monitors market developments and will issue HMA updates on a quarterly basis.

² A detailed description of the framework is available in the appendix of the [National edition](#).

In Detail

Weak evidence of overheating

Evidence of overheating of demand remained weak, even though the Montréal resale market firmed up slightly in the first quarter of 2016. This was once again due to an increase in transactions and a decrease in new listings, which caused the sales-to-new listings ratio to edge up to 54 per cent from 52 per cent in the previous quarter. Still, this ratio remained well below the problematic threshold, estimated at 70 per cent in the HMA framework (see figure 1).

Market conditions tightened in all segments³ in the first quarter of 2016, as indicated by the active listings-to-sales ratio, another measure of the gap between supply and demand. The single-family home and plex segments remained balanced but moved increasingly closer to sellers' market conditions, while the condominium segment stayed clearly favourable to buyers.

"In the first quarter of 2016, price levels remained high in relation to incomes and demographic growth, which resulted in continued moderate evidence of overvaluation in the Montréal area."



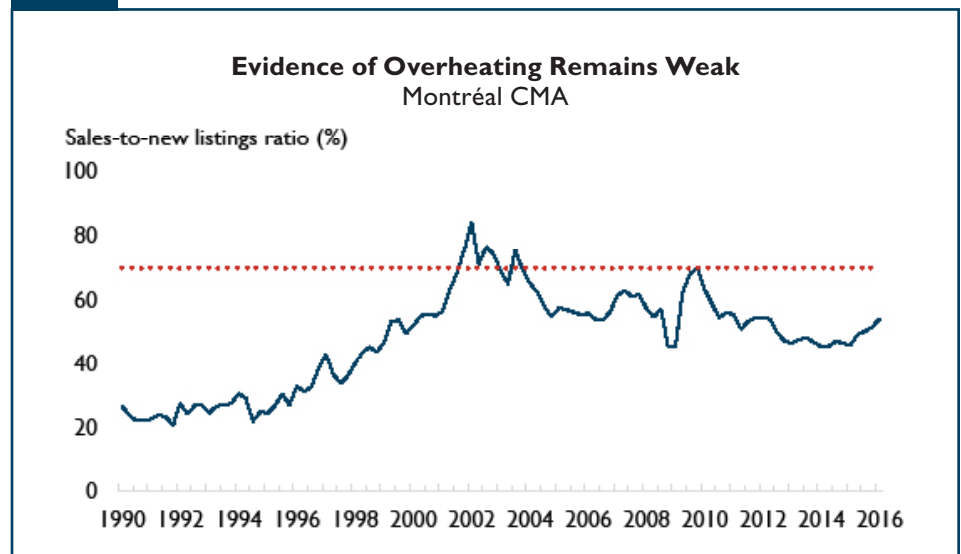
Geneviève Lapointe
Principal, Market Analysis

Market conditions varied from one sector to another across the metropolitan area, especially in the single-family home segment. On the Island of Montréal, this segment tightened, shifting from balanced to sellers' market conditions. In the suburbs, single-family home market conditions remained balanced on the North Shore, on the South Shore and in

Laval. Only the Vaudreuil-Soulanges sector still showed buyers' market conditions for this housing type. In the condominium segment, however, market conditions were favourable to buyers in all large sectors of the metropolitan area.

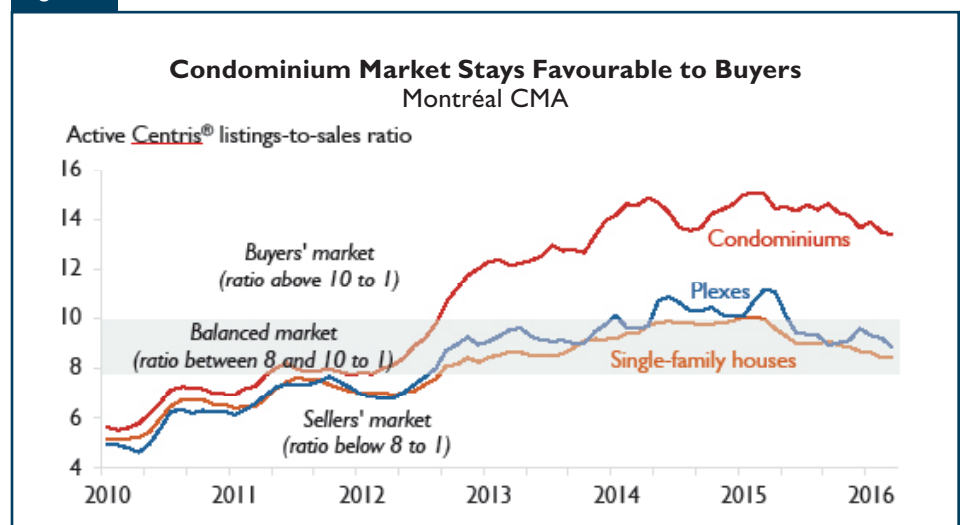
In sum, the gap between supply and demand remained rather wide on the overall resale market.

Figure 1



Source: QFREB by the Centris® system
Last data point: 2016 Q1

Figure 2



Source: QFREB by the Centris® system
Seasonally adjusted data by CMHC, three-month moving average

³ Refer to Centris® for the definitions.

Weak evidence of price growth acceleration

The gap between supply and demand remained significant on the resale market in the first quarter of 2016, even though it did narrow. The pressure on existing home prices was therefore relatively weak, and there was no indication of price acceleration in the Montréal CMA, according to the HMA.

In the first quarter of 2016, the average Centris® price of existing homes rose by 2.4 per cent over the same period in 2015.⁴ This growth was supported in part by the single-family home segment, where the average Centris® price posted a gain of 2.2 per cent. This reflected the tighter conditions in this market segment, but also a certain composition effect. The Island of Montréal, where market conditions are relatively tighter, registered the largest price increase (+4.8 per cent). Activity in this sector therefore significantly contributed to the growth in the price of single-family houses in the first quarter. The average Centris® price of condominiums, for its part, recorded almost no growth (+0.3 per cent) over the same period. This showed the abundant choice of such dwellings available to buyers on the market and put little pressure on the prices in this segment.

The Teranet–National Bank House Price Index™⁵, another indicator that takes into account composition effects, showed in March 2016 that prices in the overall Montréal area were stable from the same period in 2015. This reflected the continued

wide gap between supply and demand on the market, mentioned in the previous section.

All in all, the various price measures showed no evidence of price growth acceleration on the Montréal resale market.

Moderate evidence of overvaluation

The HMA framework continued to detect moderate evidence of overvaluation in the Montréal CMA in the first quarter of 2016. This result was due to several factors.

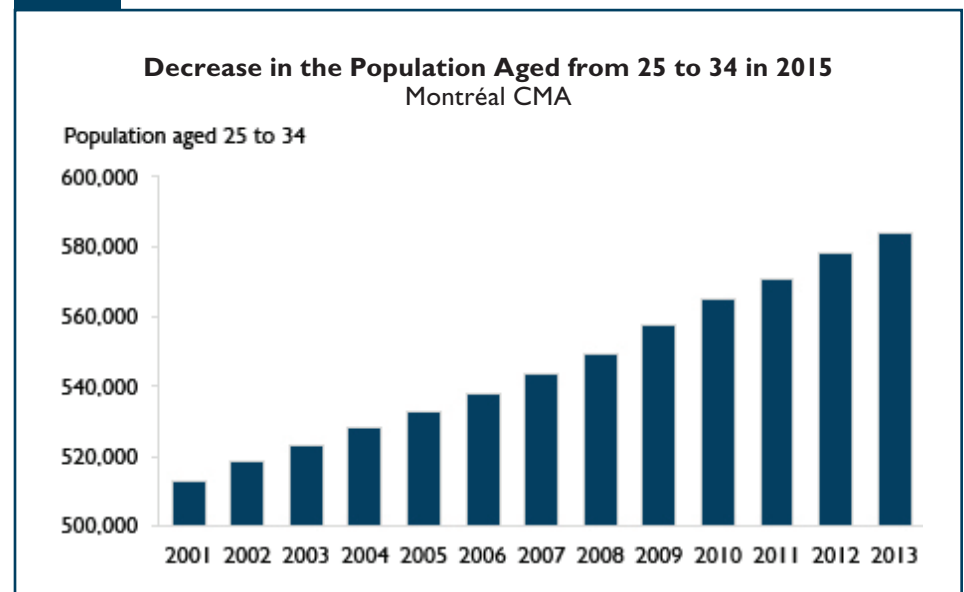
For one thing, during the 2000s, home prices experienced strong growth, while incomes and the population rose more modestly. As a result, the level of prices progressively moved away from what would have been dictated by the economic and demographic fundamentals. In the first quarter,

this gap still persisted on the Montréal market. For another, based on the HMA estimates, the downward trend in the population aged from 25 to 34 registered in 2015 continued in the first quarter of 2016. Since this group has accounted for a significant share of homebuyers in recent years, especially in the condominium segment,⁶ it is likely that this slowdown contributed to limiting housing demand on the Montréal market.

Still, the more modest growth in prices, combined with the moderate rise in incomes, helped mitigate the situation. In fact, in the first quarter of 2016, prices progressively moved closer to, without quite reaching, the level that would have been expected based on the fundamentals.

In the end, given the trends in the prices and the fundamentals, moderate evidence of overvaluation continued to be observed in the Montréal area.

Figure 3



Source: Statistics Canada, Demography Division, Population Estimates
2015: preliminary data

⁴ In the fourth quarter of 2015, the growth was 1.2 per cent over a year earlier.

⁵ The Teranet–National Bank House Price Index is based on the repeat sales methodology.

⁶ This age group accounted for a large proportion (34 per cent) of homebuyers in 2011. Source: Statistics Canada, National Household Survey, 2011.

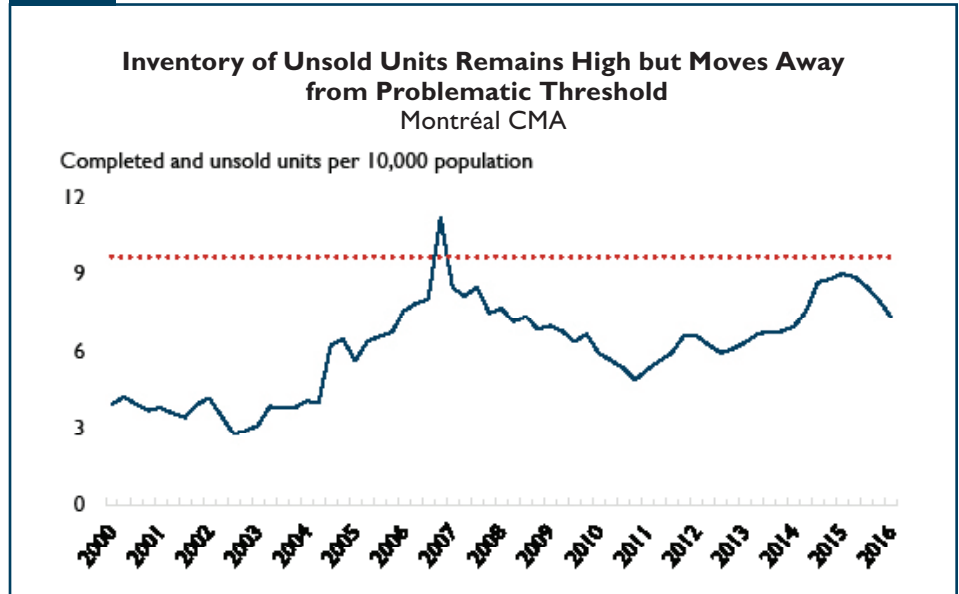
Weak evidence of overbuilding

To assess overbuilding, the framework uses the inventory of completed and unsold units per 10,000 population and the rental housing vacancy rate as indicators. In the first quarter of 2016, these two indicators were below their respective problematic thresholds. Evidence of overbuilding therefore remained weak.

The inventory of completed and unsold units per 10,000 population stayed high but did continue to decline gradually. This was essentially due to the condominium segment, since inventories of single-detached, semi-detached and row houses remained low. In fact, at the end of March 2016, the Montréal CMA had a total of 2,295 completed and unsold condominium units. However, with the slowdown in condominium construction observed in 2015 and early 2016, fewer new projects were added to the market. Under these circumstances, demand shifted more toward unsold new condominiums, which helped bring down inventory levels. In the various geographic sectors, different dynamics were at play. In fact, inventories of condominiums declined mainly on the Island of Montréal and, to a lesser extent, on the South Shore. However, these decreases were partly offset by increases in the inventories of completed and unsold units on the North Shore and in Laval.

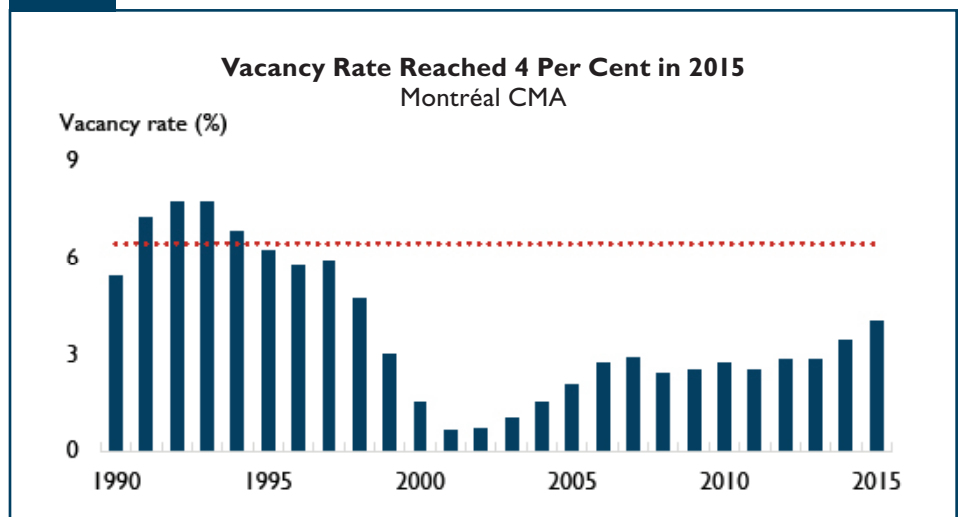
In sum, these trends helped the indicator move away from the problematic threshold, but the inventories of unsold units still remained at relatively high levels in the overall Montréal CMA.

Figure 4



Sources: Statistics Canada and CMHC
Last data point: 2016 Q1

Figure 5



Source: CMHC
Last data point: October 2015

As for the rental housing vacancy rate, this indicator did not change from the previous quarter, as this measure is taken only once a year, in October. However, as construction got under way on a large volume of rental dwellings in 2015, many units should be completed this year. In fact, according to the latest forecasts, this new supply is expected to

exceed demand on the rental market. This should result in a small increase in the vacancy rate, which should rise to 4.3 per cent at the time of the next survey in October 2016, from 4.0 per cent a year earlier.

Overview of the Housing Market Assessment analytical framework

To obtain an accurate picture of the overall state of the housing market, it is important to consider multiple data points and lines of evidence rather than relying on just one measure or indicator.

The Housing Market Assessment (HMA) analytical framework provides a comprehensive and integrated view that relies on a combination of signals from several indicators to assess housing market conditions.

Specifically, the framework considers four main factors that may provide an early indication of potentially problematic housing market conditions: (1) overheating when demand outpaces supply; (2) sustained acceleration in house prices; (3) overvaluation of house prices in comparison to levels that can be supported by housing market fundamentals (listed below);

and, (4) overbuilding when the inventory of available housing units is elevated.

For each factor, the framework tests for: (1) the presence or incidence of signals of potentially problematic conditions, but also considers; (2) the intensity of the signals, i.e. how their magnitude compares with their historical average or how consistent they are with known or suspected house price bubbles, such as for Toronto in the late 1980s and early 1990s; and, (3) the persistence of signals over time.

Generally, a situation in which we detect few signals with low intensity or lack of persistence is associated with weak evidence of problematic conditions. Conversely, as the intensity, number, and/or persistence of the signals increases, the likelihood of a factor becoming problematic increases.

The framework takes into account demographic, economic, and financial determinants of the housing market such as population, personal disposable income, and interest rates to detect potentially problematic housing market conditions. The framework also takes into account developments in both resale and residential construction markets.

The framework was developed on the basis of its ability to detect problematic housing market conditions in historical data, such as the house price bubble Toronto experienced in the late 1980s and early 1990s. The ability of the HMA to detect current problematic conditions relies on the assumption that historical relationships between prices and fundamental drivers of housing markets have not changed.

Housing Market Assessment Factors

Overheating

Overheating is caused by demand significantly and persistently outpacing the supply of housing. The sales-to-new listings ratio is used as an indicator to assess possible overheating conditions in the existing home market. To identify problematic overheating conditions, the framework compares the sales-to-new listings ratio to thresholds. When demand is strong relative to supply, house prices typically grow at a faster rate. Sustained overheating conditions on the existing home market may lead to acceleration in house prices for existing and new homes. However, as supply and demand begin to balance out, indicators of overheating (and acceleration) would begin to soften and house prices would gradually moderate.

Acceleration in House Prices

Under balanced market conditions, house prices are expected to increase over time, in line with increases in households' cost of

living. House price acceleration occurs when the growth in house prices strengthens over time on a persistent basis. Acceleration in house prices over an extended period can cause their pace of increase to depart from the overall price inflation and eventually lead to overvaluation.

To assess acceleration in house prices, the HMA framework uses a statistical test* that was developed to identify periods of accelerating asset prices.

Overvaluation

Overvaluation is detected when house prices remain significantly above the levels warranted by fundamental drivers of housing markets such as income, population, and actual and expected financing costs.

The HMA framework uses combinations of different house price measures and models to estimate house price levels warranted by fundamental drivers.

The difference between observed house prices and their estimated levels consistent with housing market fundamentals allows for an estimation of the degree of over- and undervaluation. The use of different price measures and models improves the reliability of results.

Overbuilding

Overbuilding is detected when the supply of readily available housing units significantly exceeds demand. In such a context, downward pressure on house prices would occur until the excess supply is eventually absorbed.

To assess overbuilding conditions in the housing market, the HMA framework uses two indicators that relate to the supply of readily available housing units: the rental vacancy rate, and the inventory of completed and unsold housing units per 10,000 population. The HMA framework compares the current level and recent trends in these indicators with thresholds.

Note 1: Colour codes indicate the level of evidence of problematic conditions. The HMA reflects a comprehensive framework that not only tests for the presence or incidence of signals of potentially problematic conditions, but also considers the intensity of signals (that is, how far the indicator is from its historical average) and the persistence of signals over time. Generally, low intensity and persistence are associated with a lower potential of upcoming problematic conditions. As the number of persistent signals increases, the evidence of a problematic condition developing increases.

Note 2: Results at the CMA level are not segmented by housing type or neighbourhood. They represent an assessment of the entire CMA. However, specific CMA reports provide further detailed analysis of these markets.

Note 3: The colour scale extends to red only for those factors that have multiple indicators signaling significant incidence, intensity and persistence of potentially problematic conditions. As a result, only overvaluation and overbuilding can receive a red rating, since they are assessed using more than one indicator.

Note 4: To ensure the framework is as current as possible, on a regular basis, we undertake a model selection process whereby our house price models for overvaluation are tested for statistical significance at the national and CMA level. The result of this process may change the number of indicators of a problematic condition from the previous assessment.

* See Phillips, Wu and Yu (2008) "Explosive Behaviour in the 1990s NASDAQ When Did Exuberance Escalate Asset Values?" for further details on the methodology.

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