

HOUSING MARKET ASSESSMENT

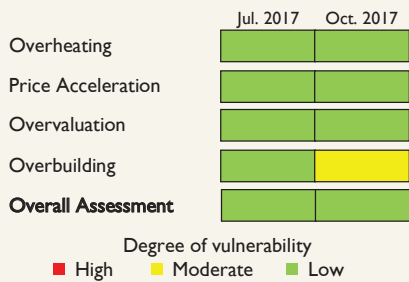
St. John's CMA

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Highlights

Results Overview St. John's CMA



- Overall, there is a low degree of vulnerability in the St. John's CMA housing market¹.
- House prices remain under pressure, due to economic weakness.
- There is moderate evidence of overbuilding based on completed and unsold homes.
- Excess supply of existing home inventory and lower sales activity has resulted in low evidence of overheating and price acceleration.

HMA Overview²

CAs Canada's authority on housing, CMHC contributes to market stability by providing information on potential imbalances that could affect housing markets. With the 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 degrees of vulnerability 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 due to 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 degrees of market vulnerability. 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 potentially low degree of vulnerability. As the number of intense and persistent signals increases, the associated degree of vulnerability increases.

In Detail

Overheating

There is low evidence of overheating in the St. John's CMA housing market. An absence of economic growth, downsizing households and low levels of custom built homes have resulted in excess inventory. This, combined with fewer home sales throughout the area has stalled growth in the market. With various housing options and price points available to them, potential home buyers continue to be patient in their purchase decision in the current buyers' market. Despite a relatively flat year-over-year change in new and active listings, a continued retraction in sales activity has resulted in the sales-to-listings ratio trending away from the threshold for vulnerable conditions.

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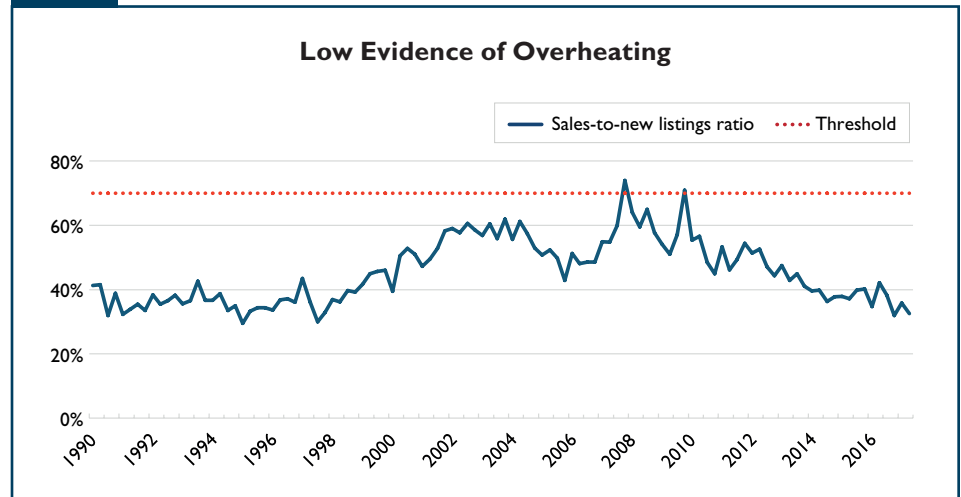
¹ Results are based on data as of the end of June 2017 and local market intelligence up to the end of September 2017. CMHC continuously monitors market developments and will issue HMA updates on a quarterly basis.

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

Price Acceleration

There is low evidence of price acceleration in the St. John's CMA housing market. An increase in the supply of homes for sale has continued to outpace demand since the end of 2012, with no average price growth over this period. No employment growth since 2014, combined with economic uncertainty and a shift to lower priced home sales have contributed to ongoing downward pressure on average prices. With many idle home builders able to react quickly to a market uptick if required, a high availability of serviced building lots and developable land will provide relief to any potential increase in future housing demand and price movement. Price adjustments have gradually kept pace with declines in economic and demographic fundamentals, especially with declines in real personal disposable income. The compositional effect of a shift to lower priced homes has also contributed to lower overall average house prices for new and existing homes.

Figure 1



Source: CREA and calculations (threshold) by CMHC. Last data point: 2017 Q2.

Overvaluation

There is low evidence of overvaluation in the St. John's CMA housing market. A negative shift in economic and demographic fundamentals, paired with lower average house prices indicates weak evidence of overvaluation in the St. John's area. Despite remaining positive, population growth is below historic rates of growth in the absence of employment and income growth in the region. Growth in house prices and income have moved in tandem historically,

but recently, declines in house prices have outpaced the decline in income on a relative basis for the first time in over a decade. This, combined with a relatively weak labour market provides further evidence of a housing market in which house prices remain under pressure and are below the threshold for vulnerable conditions.

Overbuilding

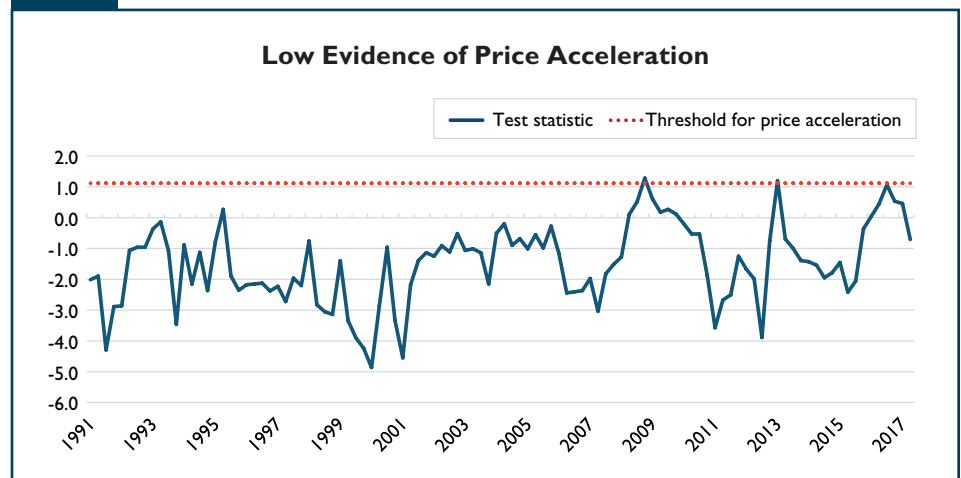
There is moderate evidence of overbuilding in the St. John's CMA housing market. The inventory of completed and unsold units relative



Chris Janes
Senior Market Analyst
(St. John's)

"There is a low degree of vulnerability in the St. John's CMA housing market. A lack of economic growth has resulted in key housing market drivers such as population, income and employment remaining flat-to-negative in 2017 and this continues to pressure housing market demand."

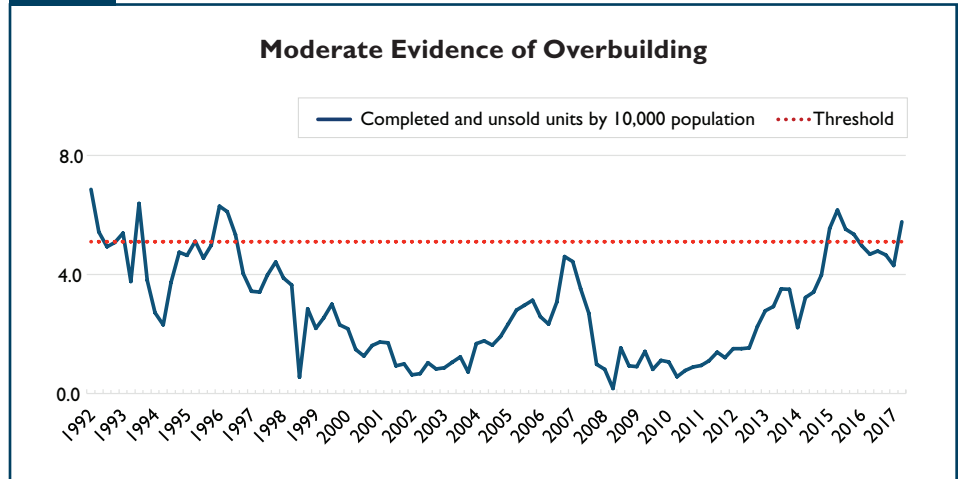
Figure 2



Source: CREA and calculations by CMHC. Last data point: 2017 Q2.

to the population increased to 5.8 from 4.3 which is now higher than the threshold of five, after being below it for over a year. Most recent numbers (August) suggest the third quarter number will be above threshold as well, but under construction units are low, which alleviates much of this concern. Under construction numbers are low due to builders holding off on new housing starts (-14% YTD) in response to lower demand for new home construction due to the weak economy. Economic uncertainty and higher completions of rental units since 2012 relative to the increase in the St. John's CMA population brought the vacancy rate up to 7.9% in October 2016, from 4.7% in the prior year. At this level, the vacancy rate is also above the threshold of 6.9.

Figure 3



Source: Statistics Canada and CMHC. Last data point: 2017 Q2.

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 detect imbalances in housing markets.

Specifically, the framework considers four main factors that may provide an early indication of vulnerability in the housing market: (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 incidence of signs of vulnerability, 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 a low degree of vulnerability. Conversely, as the intensity, number, and/or persistence of the signals increases, so does the evidence of imbalances in the housing market.

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 vulnerability. 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 vulnerable 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 vulnerabilities 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 signs of overheating, 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 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 signs of overbuilding 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 degree of market vulnerability. The HMA reflects a comprehensive framework that not only tests for the presence or incidence of signals of imbalances (that is, how far the indicator is from its historical average), but also considers the intensity and the persistence of these signals over time. Generally, low intensity and persistence are associated with a lower vulnerability. As the number of persistent signals increases, the evidence of an imbalance 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 that can identify imbalances. 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 showing vulnerability 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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