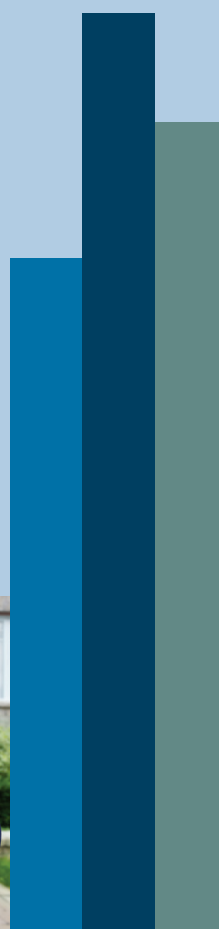


HOUSING MARKET ASSESSMENT

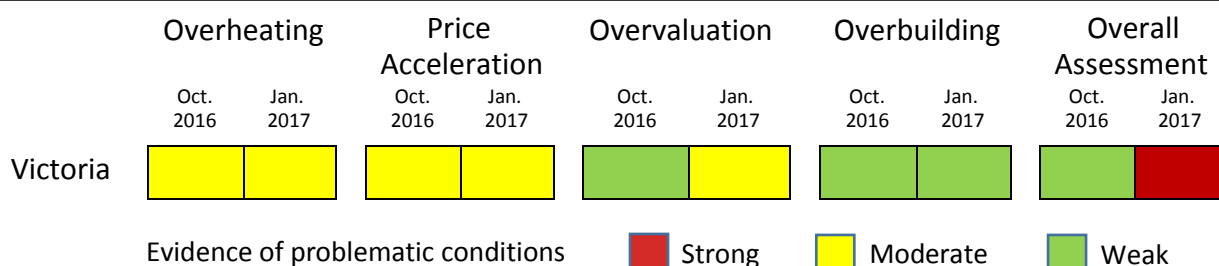
Victoria CMA

Date Released: First Quarter 2017



Housing market intelligence you can count on

Highlights



- Overall, the framework indicates strong evidence of problematic housing market conditions in the Victoria CMA¹.
- Overvaluation was detected in the Victoria CMA as price growth for housing outpaced fundamentals.
- A persistent low supply of homes in the market and elevated sales led to overheating in the market.
- With an overheated market, price growth accelerated.
- Due to low supply, there was weak evidence of overbuilding.
- 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. A brief summary of the framework is presented on page 6 of this report.

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 due to supply outpacing demand. Such an imbalance could be resolved by an adjustment in house prices. As an example, lower prices would help resolving an excess supply imbalance by supporting stronger demand and/or reducing supply. However, other unexpected development 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 September 2016 and local market intelligence up to end of December 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

Overheating

The HMA framework continued to detect moderate evidence of overheating in the Victoria CMA. The sales-to-new-listings ratio (SNLR) declined from 90 per cent in the second quarter to 80 per cent in the third quarter. The threshold for overheating is 80 per cent, and for the SNLR, 80 per cent can be considered indicative of a strong sellers' market. A typical range for a more balanced market is a SNLR somewhere between 50 to 70 per cent. In the third quarter, the movement down from a high SNLR was not the result of more supply entering the market so much as a decrease in demand. Sales trended off of a second-quarter peak but remained well above 2015 levels in the third quarter. Another measure of supply, active MLS® listings, sat at a decade's-low 979 units at the end of September, and continued to trend downward into the New Year.

Price Acceleration

Moderate evidence of price acceleration was detected in the Victoria CMA. Since the second quarter of 2015, the average MLS® price in the Victoria CMA has been an entire standard deviation above the previous three years (see figure 2). In other words,

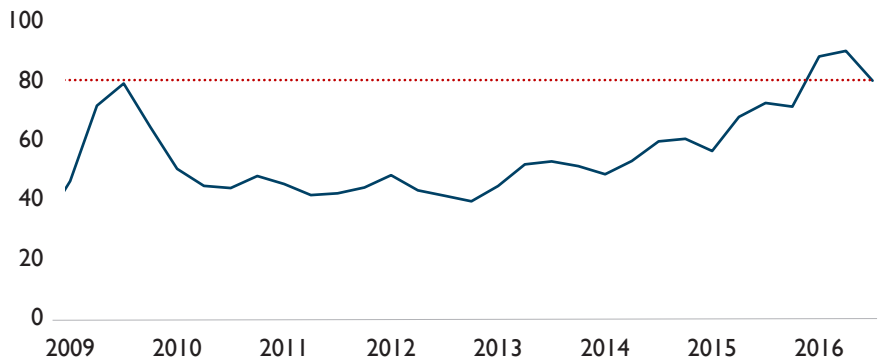
prices have been consistently rising faster than they did in the past, and by a significant margin.

Price growth has been most pronounced in single-detached homes on a year-over-year basis, but a profile of housing prices by housing type shows a different story. Since the beginning of 2016, apartment prices have moved in lock-step with single-

Figure 1

Sales-to-New-Listings-Ratio Moves Above the Threshold in Victoria

Sales-to-new listings ratio (%)



Sources: CREA and calculations (threshold) by CMHC
Last data point: 2016Q3

"Strong price growth in the Victoria CMA meant that house prices outpaced fundamentals leading the framework to detect moderate evidence of Overvaluation"

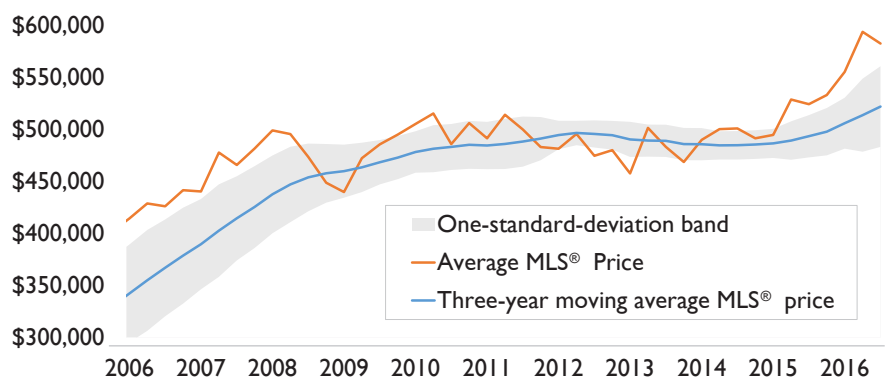


Braden Batch
Acting Senior Market Analyst (Victoria)

Figure 2

Average MLS® Prices Trend Up in Victoria

Seasonally Adjusted Average MLS® Prices

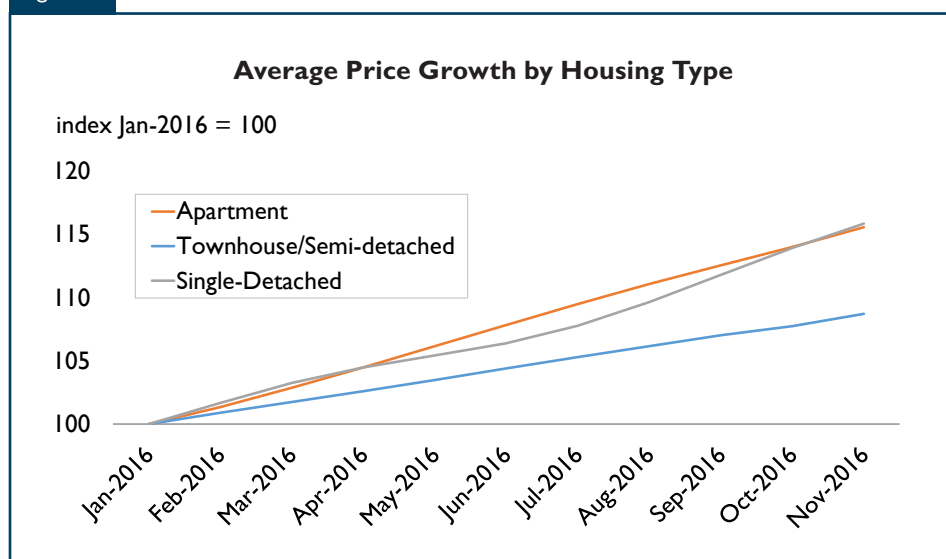


Sources: CREA
Last data point: 2016Q3

detached houses, and townhouses/semi-detached units have been increasing at roughly half the pace of other housing types (see figure 3).

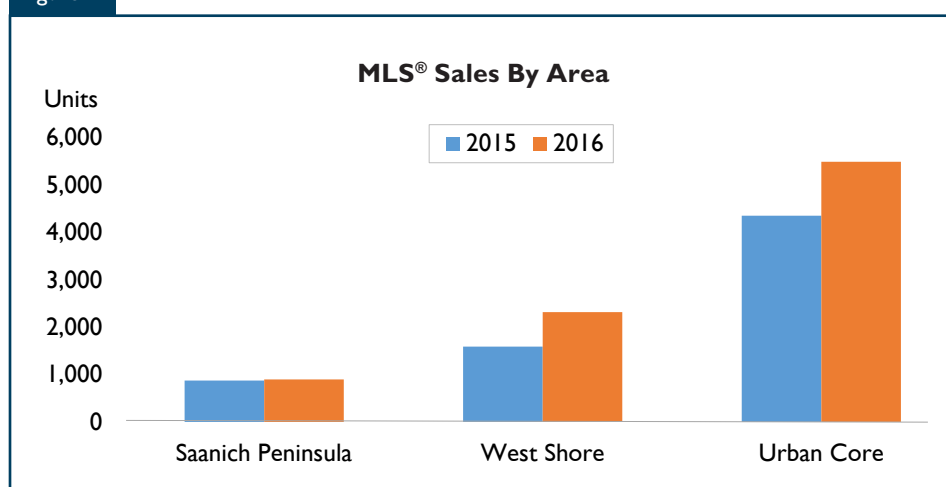
Geographically, price gains were strongest in the urban core. There remains a considerable price difference between the West Shore and the rest of the Victoria CMA. As a result, sales activity on the West Shore has been strong. West Shore total sales grew by 46 per cent year-over-year while growth in the Urban Core was 26 per cent and sales on the Saanich Peninsula were almost flat from one year to the next (see figure 4). Sales distributions alone show that there are many compositional factors to consider when interpreting movements in the average MLS® price.

Figure 3



Sources: VREB

Figure 4



Sources: VREB

Single-Detached Homes (YTD-Dec)				
Area	Average MLS® Price*	% Change from	% of Total Single-Detached MLS® Sales	
	2016	2015	2015	2016
Urban Core	\$822,077	19%	54%	51%
West Shore	\$554,990	14%	75%	72%
Saanich Peninsula	\$721,694	13%	64%	66%
Victoria CMA	\$722,111	16%	-	

Source: VREB, CMHC calculations

*Waterfront single-detached homes are not included in calculating the average MLS® price. Average MLS® prices are rounded up to the nearest thousand. December 2016 benchmark prices for single-detached homes in the Core, West Shore and Peninsula were \$758,700, \$505,000 and \$698,000 respectively.

Note: Urban Core includes Victoria (Victoria West), Esquimalt, Oak Bay, View Royal and Saanich (Saanich East/Saanich West); West Shore includes Sooke, Langford, Colwood, Metchosin, Highlands; Saanich Peninsula includes Sidney, Central Saanich, and North Saanich

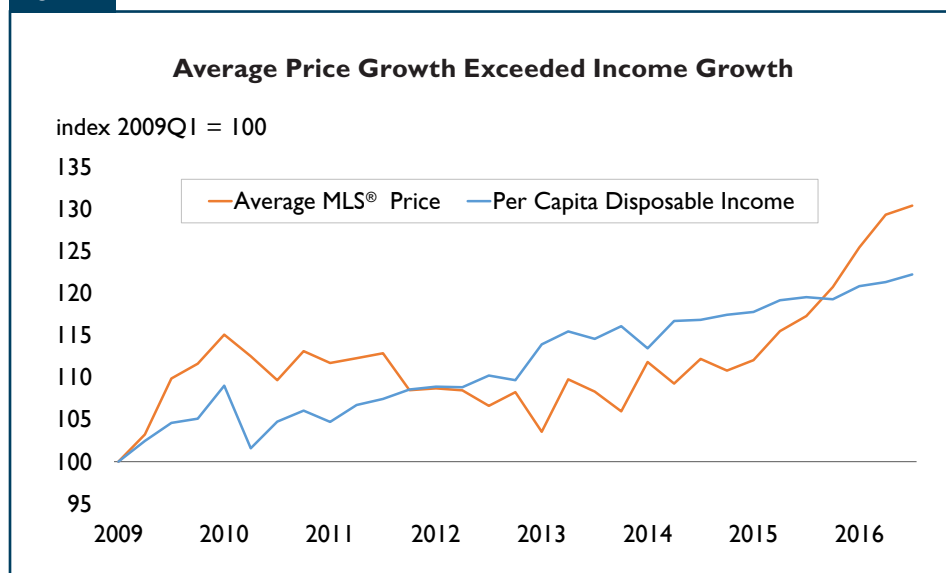
Overvaluation

The HMA framework detected moderate evidence of overvaluation in the Victoria CMA in the third quarter of 2016 as average MLS® price recorded strong price gains, price levels outpaced fundamentals. While job creation in the Victoria CMA was strong in the third quarter, it highly favoured part-time workers. At the end of September 2016, the year-over-year employment gains were 6,300 part-time jobs and 1,900 full-time jobs. Typically part-time employment is expected to support rental housing demand more so than the market for homeownership. Average disposable income in the Victoria CMA continued to be outpaced by the rise in average home prices (see figure 5). Finally, average mortgage rates increased slightly in the third quarter, meaning there was a slight decrease in credit. Without credit expansion to compensate for slower income growth, fundamentals did not keep pace with price growth.

Overbuilding

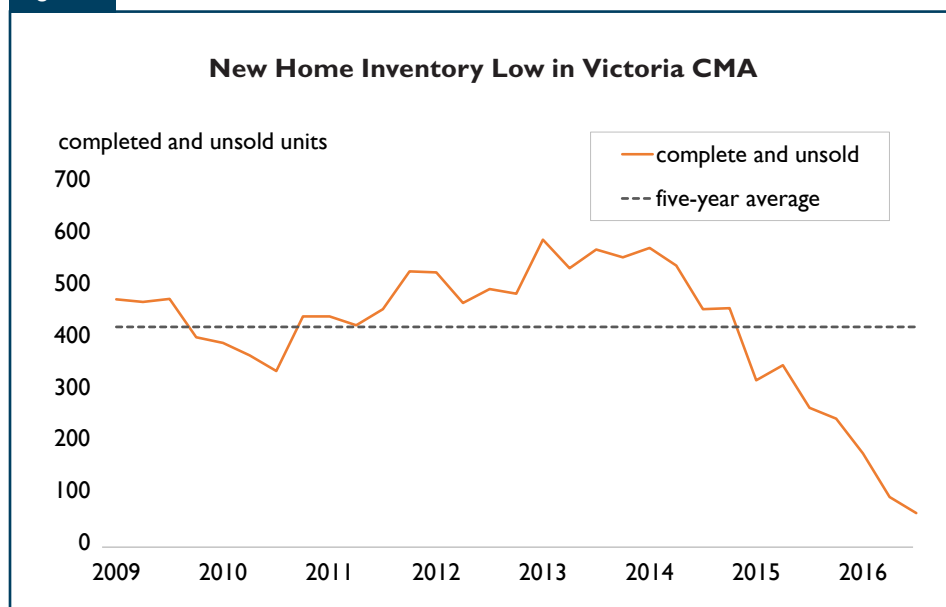
The HMA framework detected weak evidence of overbuilding in the Victoria CMA's housing market in the third quarter of 2016. In general, supply levels in the new home market mirror the low level of active listings in the existing home market. Complete and unsold units numbered just 57 at the end of the third quarter while the five-year average was 415 units (Figure 5). Similarly the October 2016 Rental Market Report showed a decline in the apartment vacancy rate from 0.6 per cent in 2015 to 0.5 per cent in 2016. Both measurements indicated low supply rather than overbuilding.

Figure 5



Sources: CREA, Conference Board of Canada
Last data point: 2016Q3

Figure 6



Sources: CMHC
Last data point: 2016Q3

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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