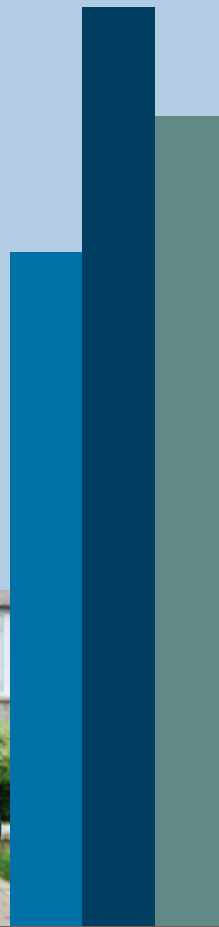


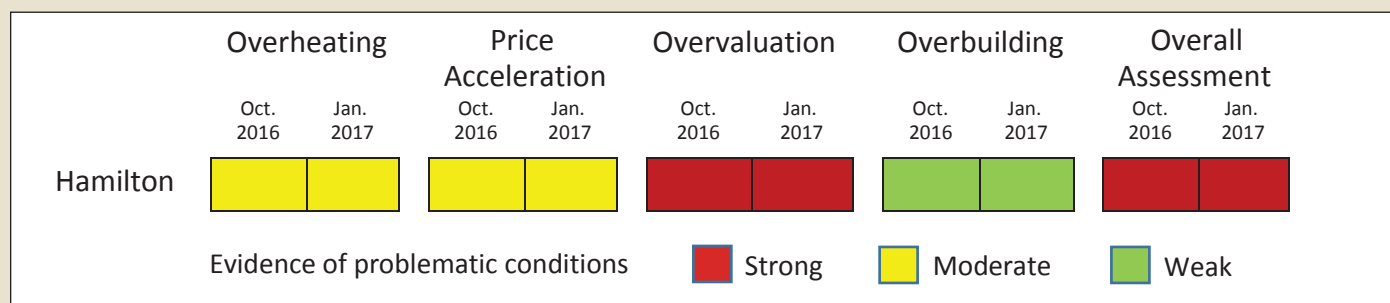
HOUSING MARKET ASSESSMENT Hamilton CMA

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Highlights



- The overall assessment¹ for the Hamilton Census Metropolitan Area (CMA) showed strong evidence of problematic conditions in Q3 2016, unchanged from the previous quarter's assessment.
- The sales-to-new-listings² ratio remained above the 75 per cent threshold used to determine evidence of overheating.
- There was moderate evidence of price acceleration in Q3 2016, based on CMHC criteria.
- In the Hamilton CMA, there was strong evidence of overvaluation in Q3 2016, as the average home price continued to increase higher than warranted by fundamental drivers of housing markets such as employment, income and population.
- There was weak evidence of overbuilding in Q3 2016.
- The Housing Market Assessment (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 Overview³

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

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 sales-to-new-listings ratio above 60 per cent is associated with sellers' market conditions. In a sellers' market, inflation adjusted home prices are generally rising. A sales-to-new-listings ratio below 40 per cent has historically accompanied inflation adjusted prices that are falling, a situation known as buyers' market. When the sales-to-new-listings ratio is between these two boundaries, the market is said to be balanced. New listings are a gauge of the supply of existing homes coming onto the market, while sales are a proxy for demand.

³ A detailed description of the framework is available in the appendix of the [National edition](#).

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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

“The Housing Market Assessment for the Hamilton Census Metropolitan Area (CMA) indicates moderate evidence of overheating, moderate evidence of price acceleration and strong evidence of overvaluation in the third quarter of 2016. The overheating assessment reflected the continued tightness of housing market conditions in the Hamilton CMA, despite a slight increase in the number of new listings during the third quarter of 2016. The average home price continued to increase at a faster pace than the rate of growth in key economic drivers such as employment, income and population. Consequently, the Housing Market Assessment (HMA) analytical framework continued to detect strong evidence of overvaluation in Q3 2016.”



Abdul K. Kargbo
Senior Market Analyst (Hamilton and Brantford CMAs)

evidence of problematic conditions. As the number of intense and persistent signals increases, the associated evidence of problematic conditions becomes stronger.

In Detail

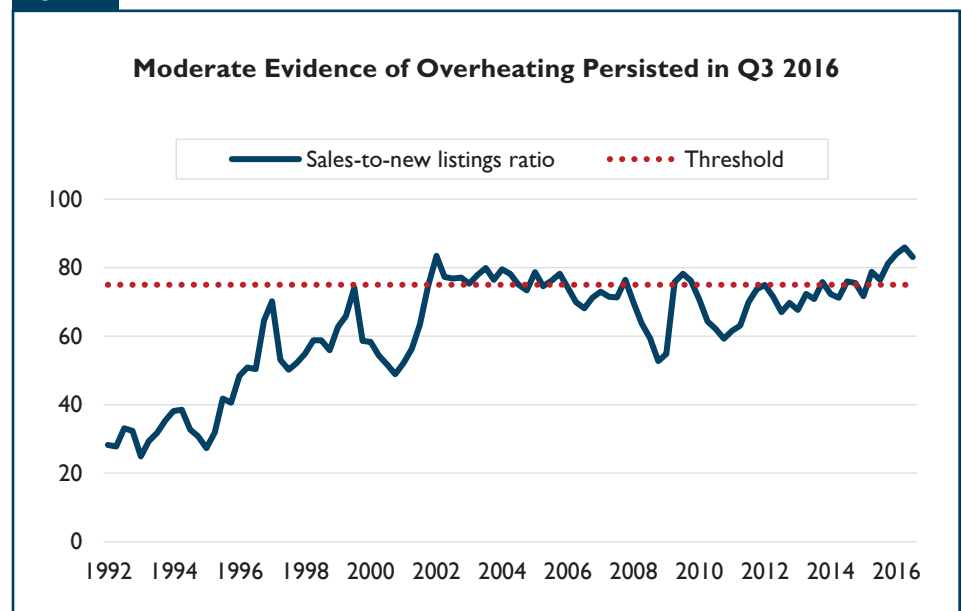
Overheating

The sales-to-new-listings ratio (SNLR) was 83 per cent in Q3 2016, down from 86 per cent in Q2 2016 on a seasonally adjusted basis. Despite the decline in Q3 2016, the SNLR remained significantly above the 75 per cent threshold used to identify evidence of overheating. The decline in the SNLR occurred because sales were practically unchanged while the number of new listings was up 2.5 per cent in Q3 2016 compared to the previous quarter on a seasonally adjusted basis. At 83 per cent, the sales-to-new-listings ratio is associated with sellers' market conditions, a situation where inflation adjusted home prices are generally rising.

Since Q1 2011, the SNLR in Hamilton has consistently indicated that sales are strong at any level of listings, putting upward pressure on house prices. Many baby boomers are likely not moving and by extension limiting the number of new listings. The increase in the average vacancy rate was probably a result of an increase in the number of rental households moving into homeownership, pushing the SNLR up even further. First-time buyer demand has been the engine for existing home sales in Hamilton since 2009. The strong presence of first-time buyers in the housing market continued to allow repeat buyers to trade up.

Townhouses continued to exhibit the tightest market conditions with a seasonally adjusted sales-to-new-listings ratio of 95 per cent in Q3 2016. Strong first-time buyer demand continued to support townhouse sales. The growth of sales of existing single-detached homes, semi-detached homes and condominium apartments outpaced the growth in new listings for this

Figure 1



Source: CREA, CMHC analysis. Last data point: Q3 2016

group of dwellings, pushing the overall seasonally adjusted sales-to-new-listings ratio above the threshold of 75 per cent in Q3 2016. All submarkets across the Hamilton CMA remained in sellers' market territory in Q3 2016.

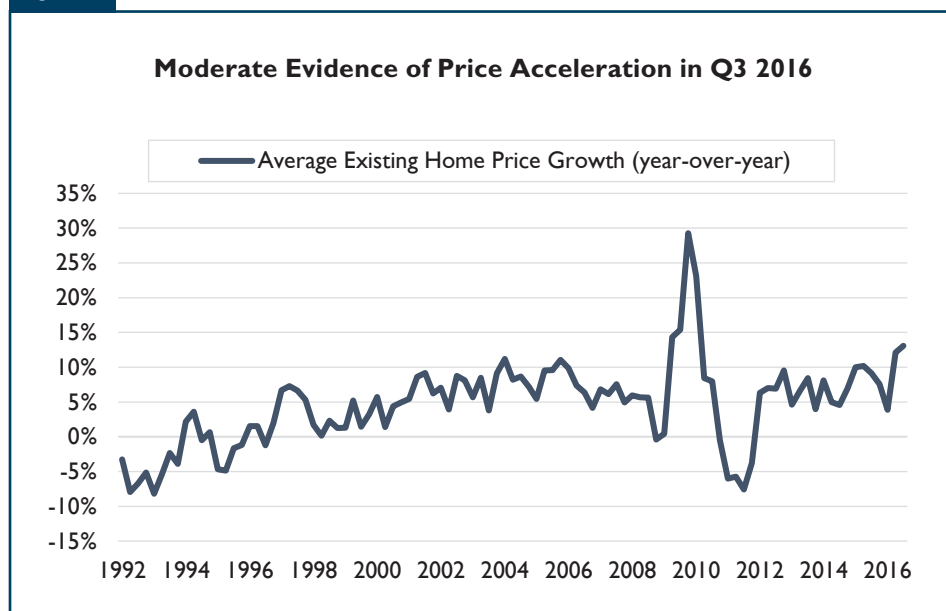
Price Acceleration

The indicator of house price acceleration remained above the critical threshold in Q3 2016. As a result, the HMA analytical framework detected moderate evidence of price acceleration in Hamilton's housing market. Strong sellers' market conditions persisted in Q3 2016 and pushed the rate of change in the average house price to move above the critical threshold.

On a seasonally adjusted basis, the average existing home price was up 1.5 per cent in Q3 2016 compared to Q2 2016 when the average existing home price registered its strongest quarterly growth since the second quarter of 2009. Seasonally adjusted prices were up across all dwelling types in Q3 2016 compared to Q2 2016. For the entire Hamilton CMA, the quarterly seasonally adjusted annual rate (SAAR)⁴ of the average existing home price was up approximately six per cent in Q3 2016 compared to Q2 2016.

The year-over-year average existing home price was up 14.1 per cent in September 2016 compared to September 2015. The Teranet⁵ – National Bank National Composite House Price Index™ was up 13.1 per cent during the same 12-month period.

Figure 2



Source: CREA, CMHC analysis. Last data point: Q3 2016

Overvaluation

In the Hamilton CMA, the average home price continued to grow faster than what would be consistent with the growth in fundamental drivers such as population, employment and income. Specifically, Hamilton's employment was practically unchanged in Q3 2016 while the average existing home price increased by 1.5 per cent compared to Q2 2016. A downward trend in employment growth generally results in slower income gains, and indeed, average weekly earnings in Q3 2016 declined 1.5 per cent compared to the previous quarter on a seasonally adjusted basis. Weak employment and slow population growth combined with a decline in income resulted in continued persistence of overvaluation in Q3 2016.

Although the rate of growth in total employment has slowed in recent months, net intra-provincial migration likely remained positive in Q3 2016 as the house price gap between the Greater Toronto Area (GTA) and the Hamilton CMA continued to attract more out-of-town buyers. The supply of low rise homes in the GTA has been limited which helps explain the increase in demand for these types of dwellings in Hamilton. Specifically, the average existing home price in the Hamilton CMA was \$501,554 in Q3 2016, compared to an average existing home price of \$738,995 in the Toronto CMA. This translates to a house price gap of \$237,441 between Toronto and Hamilton. On average, the house price gap was \$179,553 in 2015 and \$160,125 in 2014. Consequently, many potential

⁴ By removing seasonal ups and downs, seasonal adjustment allows for comparison of adjacent quarters. The quarterly SAAR indicates the annual rate of price growth that would be obtained if the same pace of quarterly price growth was maintained for four quarters. This facilitates comparison of the current rate of price growth to annual forecasts as well as to historical annual rates.

⁵ The Teranet–National Bank National Composite House Price Index™ is an independent representation of the rate of change of Canadian single-family home prices (including resale homes). The measurements are based on the property sales records of public land registries. The monthly indices currently cover Victoria, Vancouver, Calgary, Edmonton, Winnipeg, Hamilton, Toronto, Ottawa-Gatineau, Montréal, Québec City and Halifax, which are then combined to form a coast-to-coast composite index.

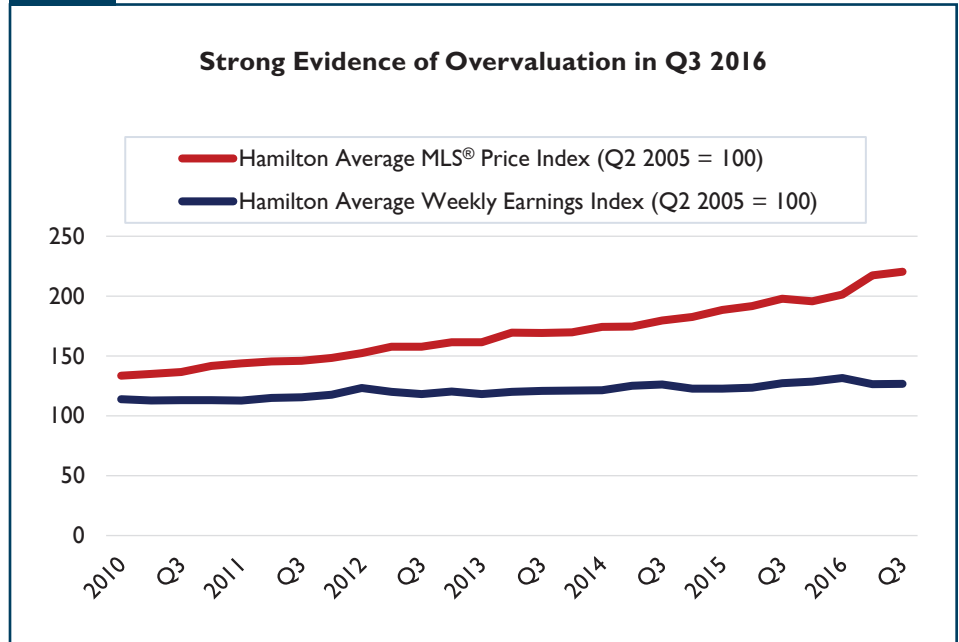
buyers that are priced out of the GTA market may be encouraged to move into the Hamilton area in search of affordable homes, particularly for low rise dwellings.

Overbuilding

The HMA analytical framework detected weak evidence of overbuilding in Hamilton's housing market in Q3 2016, unchanged from the previous quarter's assessment. The number of completed and unsold units was down in Q3 2016, primarily due to strengthening demand for multi-unit housing. The total number of completed and unsold units peaked in the fourth quarter of 2015 and has been trending down since the first quarter of 2016. Despite the strong increase in 2015, the new home inventory level remained below the threshold at which the framework would detect evidence of overbuilding.

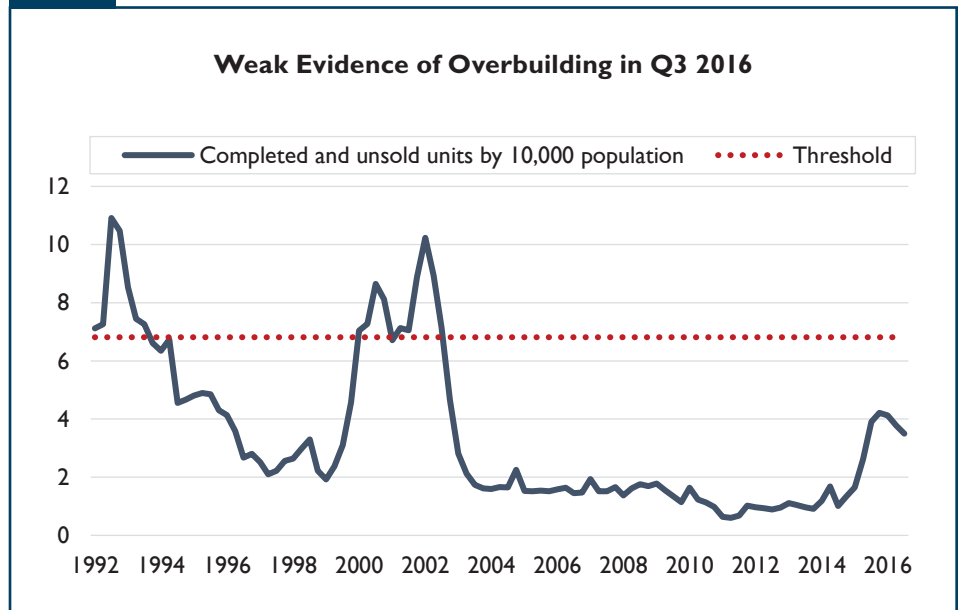
The rental vacancy rate indicator remained below the threshold at which the framework identifies evidence of overbuilding, despite the average rental vacancy rate increasing to 3.8 per cent in October 2016, from 3.4 per cent in October 2015. Weak employment growth among young adults and strong rental supply growth exerted upward pressure on vacancy rates in October 2016. Another factor that contributed to the higher vacancy rates in 2016 was that many rental households probably vacated their units and moved into homeownership, as mortgage rates remained at relatively low levels.

Figure 3



Source: Statistics Canada; CREA; CMHC analysis. Last data point: Q3 2016

Figure 4



Source: CMHC. Last data point: Q3 2016

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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