

HOUSING MARKET ASSESSMENT

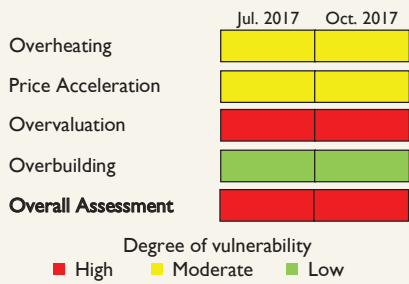
Hamilton CMA

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Highlights

Results Overview Hamilton CMA



- The overall assessment¹ for Hamilton showed the housing market displayed a high degree of vulnerability in Q2 2017, unchanged from the previous quarter's assessment.
- Evidence of overheating remained moderate since the sales-to-new-listings² ratio was persistently above the threshold for eight consecutive quarters prior to Q2 2017.
- Evidence of price acceleration remained moderate, as growth in the average MLS^{®3} sale price was much higher than the general rate of inflation.
- Evidence of overvaluation remained high, as house prices remained much higher than would be consistent with financial, economic and demographic fundamentals.

HMA Overview⁴

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 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

Moderate Evidence of Overheating

The seasonally adjusted sales-to-new-listings ratio in Hamilton was 63% in Q2 2017, below the 75% threshold for overheating. However, moderate evidence of overheating was still detected, as the sales-to-new-listings ratio was persistently above the threshold for eight consecutive quarters prior to Q2 2017. Very strong price growth in

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 sales-to-new-listings ratio above 65% is associated with sellers' market conditions. In a sellers' market, inflation adjusted home prices are generally rising. A sales-to-new-listings ratio below 45% 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 Multiple Listing Service[®] (MLS[®]) is a registered trademark of the Canadian Real Estate Association (CREA)

⁴ A detailed description of the framework is available in the appendix of the [National edition](#).

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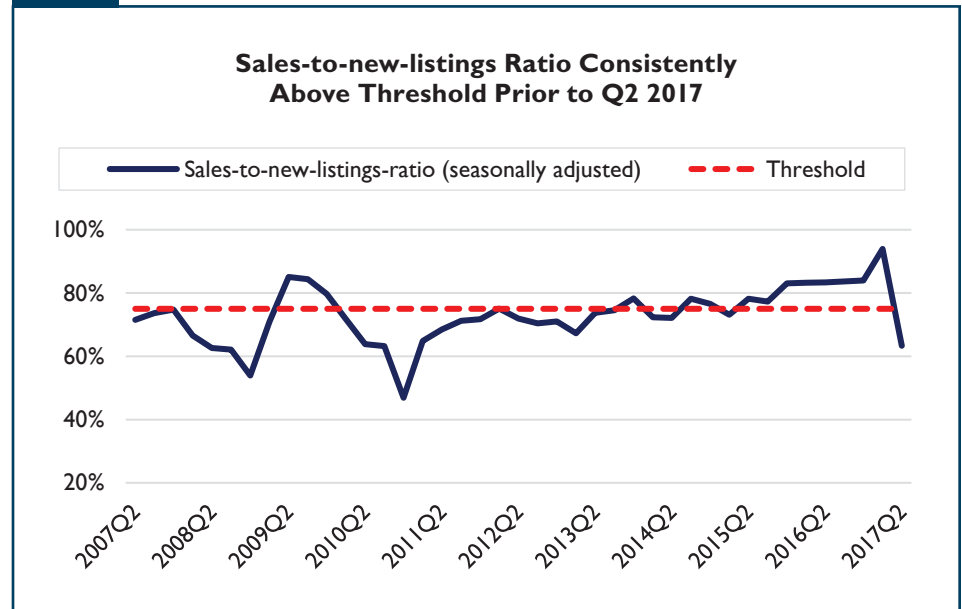
Q1 2017 led to a much higher number of new listings in Q2 2017. MLS® sales were lower as many potential buyers were unwilling to pay the high prices on homes listed for sale. The Ontario Fair Housing Plan likely created less urgency among buyers to act while encouraging more vendors to list their home for sale.

Sales-to-new-listings ratios for each dwelling type were all significantly lower in Q2 2017 than in Q1 2017. Only the sales-to-new-listings ratio for apartments remained above the threshold for overheating in Q2 2017. Sales-to-new-listings ratios for apartments, detached homes and townhomes were all above the threshold in Q1 2017. The market for apartments still favoured sellers in Q2 2017, as new listings decreased along with sales. New listings increased and sales decreased for all other dwelling types. The lowest sales-to-new-listings ratio in Q2 2017 was for detached homes

at approximately 60%, indicating balanced market conditions for that dwelling type. Data for Q3 2017 show the market for detached homes

and townhomes remained balanced, while the market for apartments still favoured sellers.

Figure 1



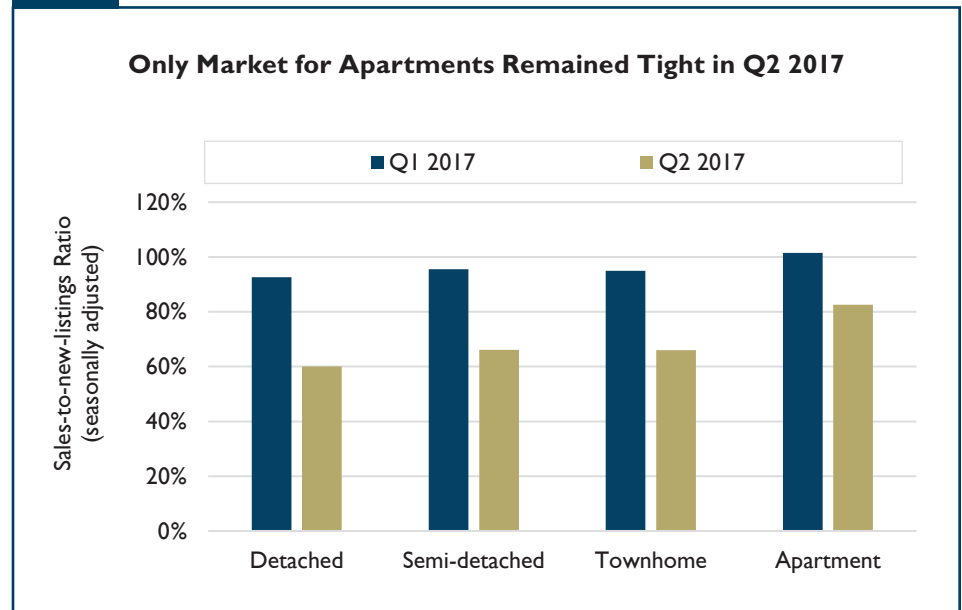
Source: CREA, CMHC calculations. Last data point: Q2 2017



Anthony Passarelli
Senior Market Analyst

"The HMA framework continued to detect a high degree of vulnerability in the Hamilton housing market in the second quarter of 2017, primarily due to high evidence of overvaluation. House prices in Hamilton continued to grow quickly and remained much higher than levels supported by economic and demographic fundamentals, such as personal disposable income and population growth."

Figure 2



Source: Ontario Regional MLS® Database, CMHC calculations. Last data point: Q2 2017

Moderate Evidence of Price Acceleration

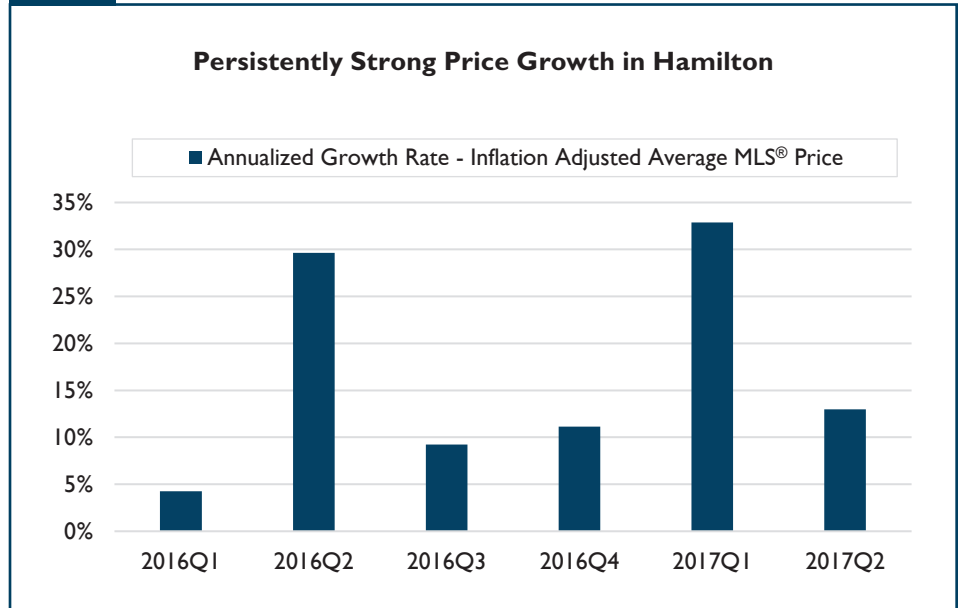
Moderate evidence of price acceleration was detected in Hamilton in Q2 2017, as growth in the average MLS® price continued to be much higher than the general rate of inflation. Following adjustment for inflation, the average MLS® price grew at an annualized rate of 13%. Price growth in Q2 2017 was higher than what typically occurs in a balanced market in Hamilton, which is characterized by a sales-to-new-listings ratio between 45% and 65%. The average MLS® price was skewed to the upside by the composition of sales. Homes with greater than 2000 square feet of living space, which are generally more expensive than homes with a smaller living space, made up a much larger percentage of total MLS® sales in Q2 2017 than in Q1 2017. One of every five MLS sales in Hamilton in Q2 2017 were of homes with greater than 2000 square feet of living space, compared to one of out of every six MLS sales in Q1 2017.

The average MLS® price decreased from Q2 2017 to Q3 2017, despite balanced market conditions. Again, the composition of sales had a significant impact on the average price, but this time homes with greater than 2000 square feet of living space made up a smaller percentage of transactions than in the previous quarter. Also, a smaller percentage of transactions in Q3 2017 occurred in two of Hamilton's three most expensive markets, Ancaster and Waterdown. The share of transactions occurring in Burlington was steady.

High Evidence of Overvaluation

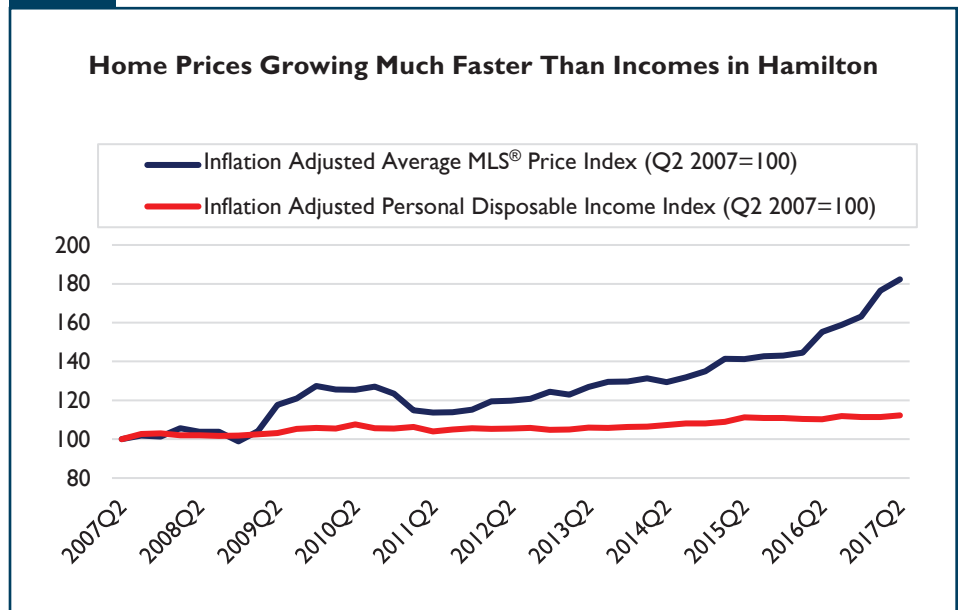
High evidence of overvaluation persisted in Q2 2017, as home prices remained much higher than levels

Figure 3



Source: CREA, Statistics Canada, CMHC calculations. Last data point: Q2 2017

Figure 4



Source: CREA, Conference Board of Canada, Statistics Canada, CMHC calculations. Last data point: Q2 2017

supported by financial, economic and demographic fundamentals. Double-digit annual growth rates in a number of house price measures for Hamilton continued to far outpace growth rates of real personal disposable

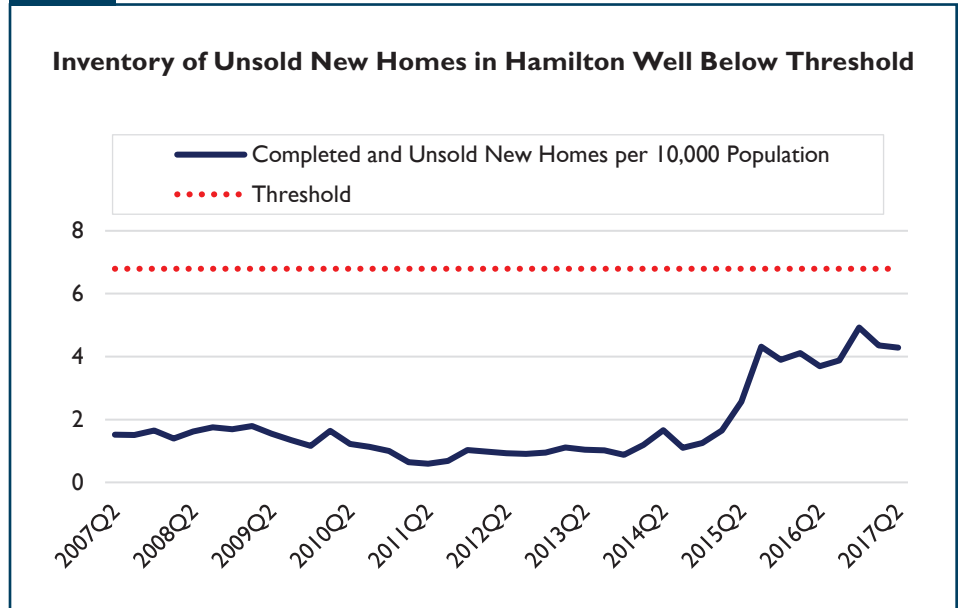
income per capita, employment and the young adult population 25 to 34 years of age.

Real personal disposable incomes grew in Hamilton, supported by higher full-time employment. The

ratio of full-time to part-time jobs increased to a fairly high level, putting upward pressure on overall average weekly earnings. However, despite healthy income gains in Q2 2017, real personal disposable incomes have increased by just 12% over the ten years ending in Q2 2017, whereas the inflation adjusted average MLS® price increased by roughly 80% in the same period.

The population 25 to 34 years old is a fundamental driver of housing demand in Hamilton, as they make up the largest share of first-time buyers in that market. The annualized growth rate of Hamilton's population 25 to 34 years of age remained strong in the 2.5% to 3.0% range in Q2 2017. Despite house prices decreasing in the GTA from Q1 2017 to Q2 2017, a significant number of 25 to 34 year olds from there continued to migrate to Hamilton in search of more affordable housing options, particularly low-rise homes. In Q2 2017, a household income of \$135,000 was required⁵ to purchase the average-priced resale detached home in Hamilton, lower than the \$145,000 household income required to purchase the average-priced resale townhome in the GTA. However, strong population growth in that age group was not enough to account for current price levels.

Figure 5



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

Low Evidence of Overbuilding

Both the number of completed and unsold new homes per 10,000 population and the rental vacancy rate remained at levels that indicated weak evidence of overbuilding. After adjusting for regularly occurring seasonal variation, the number of completed and unsold new homes per 10,000 population decreased slightly from Q1 2017 to Q2 2017. The inventory consisted mostly of townhomes, with the majority of them located in Waterdown.

In every quarter since Q2 2015, less than half of new townhomes in Hamilton were sold by the

time they were completed, which could have led to a large unsold inventory. Spillover demand from the resale market helped to keep new townhome inventories manageable, as listings were very scarce from Q2 2015 to Q2 2017. Seasonally adjusted data for Q3 2017 show that inventories of unsold new homes continued to decrease in Hamilton, including new townhomes. However, demand has softened and buyers now have far more options in the resale market, posing a greater risk that new home inventories will rise if a similar percentage of townhomes currently under construction are unsold at completion.

⁵ Based on average MLS® price by dwelling type, 95% loan-to-value mortgage, 25 year amortization, 4.64% qualifying mortgage rate and 32% gross-debt-service ratio.

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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