HOUSING MARKET INFORMATION

HOUSING MARKET ASSESSMENT
Hamilton CMA

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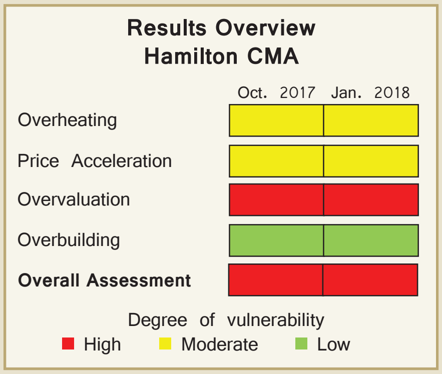
Canada

CMHC SCHL

Highlights



- The overall assessment[1] for Hamilton showed the housing market displayed a high degree of vulnerability in Q3 2017, unchanged from the previous quarter's assessment.
- While the sales-to-new-listings[2] ratio was below the threshold in Q3 2017, evidence of overheating remained moderate since the sales-to-new-listings ratio was above the threshold in two of the past four quarters.
- While Hamilton house prices decreased from Q2 2017 to Q3 2017, evidence of price acceleration remained moderate as price growth far exceeded the general rate of inflation for a number of consecutive quarters prior to Q3 2017.
- Evidence of overvaluation remained high, as house prices remained much higher than would be consistent with financial, economic and demographic fundamentals.

HMA Overview[3]

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 was 59% in Hamilton in Q3 2017, below the 75% threshold for overheating. However, moderate evidence of overheating was still detected, since the sales-to-new-listings ratio was above the threshold in two of the past four

[1] Results are based on data as of the end of September 2017 and local market intelligence up to end of December 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.

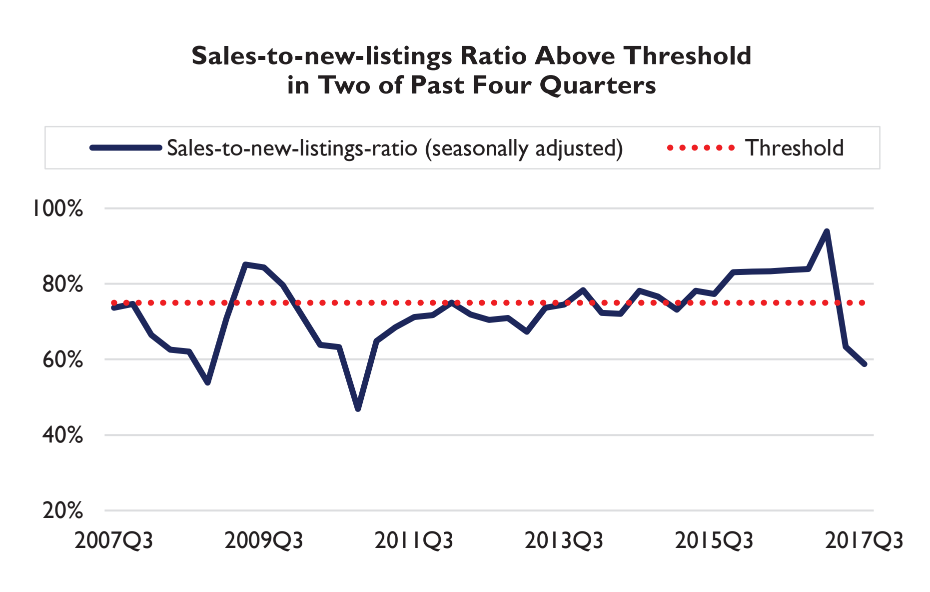
[3] A detailed description of the framework is available in the appendix of the National edition.

quarters. The sales-to-new-listings ratio decreased slightly from Q2 2017 to Q3 2017, as sales declined more than new listings. A growing number of potential buyers stayed on the sidelines in Q3 2017 due to a lack of affordable options for purchase and the expectation that prices may decrease in the near future. While new listings remained elevated versus recent history, fewer homeowners listed their home in reaction to demand softening in Q2 2017.

The sales-to-new-listings ratios of each dwelling type decreased from Q2 2017 to Q3 2017 and none of them were above the threshold for overheating. The apartment market remained in seller's territory, as listings continued to be very scarce and demand held up better than for other dwelling types due to affordability. The market for single-detached homes, as well as semi-detached and townhomes was balanced in Q3 2017.

Timelier data for Q4 2017 shows that the sales-to-new-listings ratios of each dwelling type increased, with the exception of apartments which remained relatively steady. Overall, sales outpaced new-listings as a number of buyers came off the sidelines to buy before tougher mortgage qualification rules came into effect in January 2018. Strong employment growth in 2017 also contributed to greater demand.

Figure 1

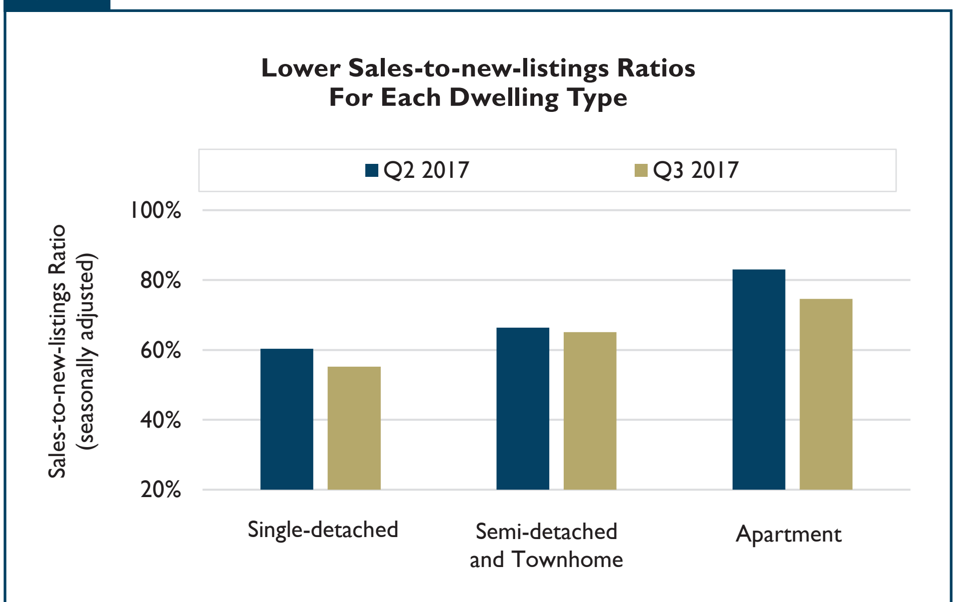


Source: CREA, CMHC calculations. Last data point: Q3 2017

Anthony Passarelli
Senior Market Analyst

"The HMA framework continued to detect a high degree of vulnerability in the Hamilton housing market. The assessment was primarily due to evidence of overvaluation remaining high. While Hamilton house prices decreased from the second quarter to the third quarter, they remained much higher than levels supported by economic and demographic fundamentals, such as average personal disposable income and population growth."

Figure 2



Source: Ontario Regional MLS® Database, CMHC calculations. Last data point: Q3 2017

Moderate Evidence of Price Acceleration

While Hamilton house prices decreased from Q2 2017 to Q3 2017, evidence of price acceleration remained moderate as price growth far exceeded the general rate of inflation for a number of consecutive quarters prior to Q3 2017. The average MLS®[4] price does not typically decrease in a balanced market, which in Hamilton is characterized by a sales-to-new-listings ratio between 45% and 65%. The average MLS® price was skewed significantly to the downside by the composition of sales. A much smaller percentage of sales were of pricier homes, with just one of every five sales in Q3 2017 having a purchase price of $700,000 or greater compared to one of every four sales in Q2 2017.

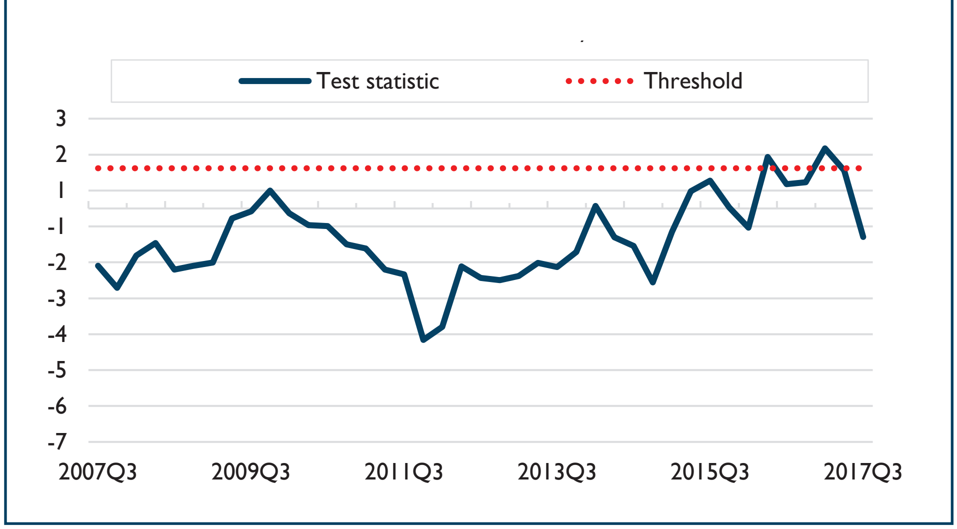
The average MLS® price was relatively steady from Q3 2017 to Q4 2017, despite the market almost tipping back into seller's market territory. Again, the composition of sales had a significant impact on the average price, as a smaller percentage of sales in Q4 2017 had a purchase price of $700,000 or greater compared to Q3 2017. More buyers turned their attention towards less expensive homes, as evidenced by tight markets for apartments and townhomes.

High Evidence of Overvaluation

While Hamilton house prices decreased from the second quarter to the third quarter, they remained much higher than levels supported by financial, economic and demographic fundamentals. For a prolonged period of time prior to the third quarter, growth rates of real personal disposable income per capita, employment and the young adult population 25 to 34 years of age were significantly detached from growth rates of a number of house price measures for the region.

Figure 3

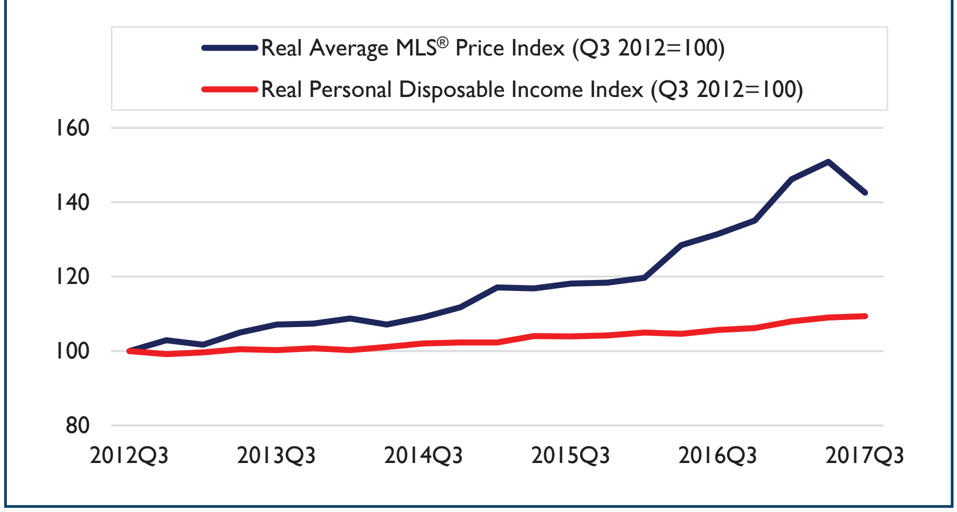
Price Acceleration Detected Recently in Hamilton



Source: CREA, CMHC calculations. Last data point: Q3 2017
Note: The test is done using the MLS® average price. Other price indices are also monitored.

Figure 4

House Prices Have Grown Much Faster Than Incomes in Hamilton



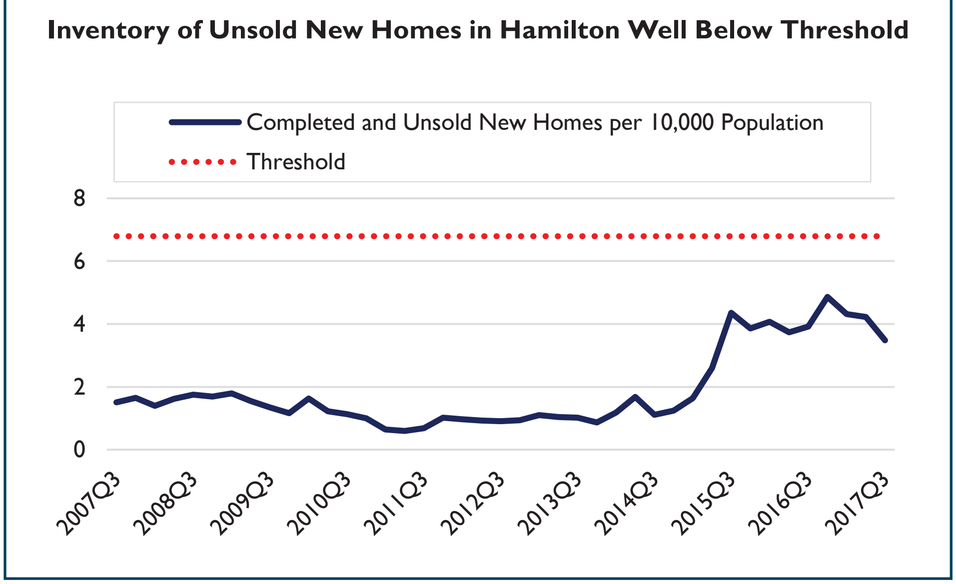
Source: CREA, Conference Board of Canada, Statistics Canada, CMHC calculations.
Last data point: Q3 2017

[4] Multiple Listing Service® (MLS®) is a registered trademark of the Canadian Real Estate Association (CREA).

Real personal disposable incomes outpaced real house prices in Hamilton for the first time since Q2 2015, helping to reduce overvaluation. Real personal disposable incomes grew in Hamilton for the fifth consecutive quarter, supported by higher full-time employment. The ratio of full-time to part-time jobs increased to a high level, putting upward pressure on incomes. More jobs in higher paying industries such as construction and professional services also contributed to income growth.

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 Q3 2017. Despite house prices decreasing in the GTA for the second consecutive quarter, 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. 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: Q3 2017

Low Evidence of Overbuilding

Both the number of completed and unsold new homes per 10,000 population and the rental apartment vacancy rate were 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 from Q2 2017 to Q3 2017 and was well below the threshold. New home inventories decreased as fairly weak demand still managed to outpace the low supply of newly completed unsold homes. The largest inventory reduction occurred in Stoney Creek. Most of the remaining unsold inventory consisted of townhomes, with the largest concentration located in Waterdown.

Inventories increased from Q3 2017 to Q4 2017 but remained relatively low. The primary reason for the increase was a number of unsold apartments completed in Burlington. Townhome inventories were significantly lower due to greater demand. Townhome inventories decreased in Waterdown, Glanbrook, Stoney Creek and Hamilton Mountain.

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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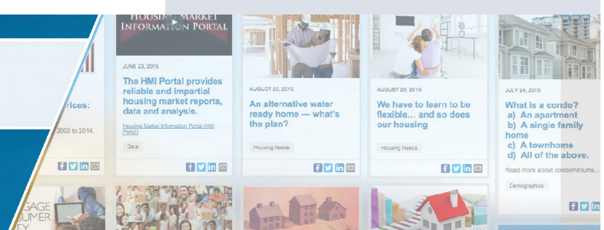

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