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Homebuyers' Market Perceptions and Risk Attitudes: Results from the 2018 Homebuyers' Motivations Survey

Executive summary

The aim of this report is to present the highlights of the Homebuyers' Motivations Survey conducted in Vancouver, Toronto and Montréal in the fall of 2018. The survey was developed as a complementary piece to traditional economic analysis with a focus to gain a better understanding of additional factors influencing rapid price growth in some markets in Canada. As such, the report focuses on the subjective factors influencing homebuyers in their purchases.

This year, we focused on expectations of price growth and on changes in those expectations. In addition, five main facts are highlighted in this report:

- In Montréal, the proportion of homebuyers who said they spent more than they budgeted increased from 24% in 2017 to 28% in 2018. In addition, the proportion of homebuyers who perceived foreign investors have a lot of influence on house prices in Montréal rose from 42% to 52%.
- A large majority of homebuyers are less willing to take financial risks (75%).¹
- The proportion of homebuyers who experienced a bidding war in Toronto dropped by 10 percentage points between 2017 and 2018 (from 55% to 45%).
- Fundamentals drivers (interest rate changes, employment growth, population growth) are thought by homebuyers as having less impact on house prices than factors linked to speculation².
- Price growth expectations in one year were quite similar to the actual price changes the year before, except in Montréal where price growth expectations in 2018 were lower than the actual changes in 2017.

Introduction

The Toronto and Vancouver census metropolitan areas (CMAs) face severe housing affordability issues. According to a recent CMHC report examining house price escalation (2018), demand-side variables such as income, population and interest rates cannot entirely explain rising prices.³ As a result, our understanding of housing markets can benefit from analyzing how subjective factors influence price growth. Recent studies of price expectations show that exuberant optimism can lead at times to speculation and distort the fundamental prices of housing.^{4,5}

Results presented following the 2017 survey were focused on the following key areas: the characteristics of homebuyers who participated in a bidding war, the relationship between homebuyers' purchase budget and the choices made before their purchase and, finally, the impact of social influences and perceptions on home prices.⁶

This year, the report focuses on the subjective factors influencing purchase behaviours and housing demand. By examining those subjective factors, for instance, the composition of price expectations and the risk profile of respondents, the survey shows that fundamentals drivers (interest rate changes, employment growth, population growth) are thought by homebuyers as having less impact on house prices than factors linked to perception. The fact that those perceived factors, linked to speculation, have a greater influence on house prices can lead to higher house price growth expectations because it makes homebuyers more willing to pay higher for homes.

Finally, an analysis of purchase behaviours compares some characteristics of homebuyers involved in bidding wars in 2018 with some of the results from the 2017 report.

"The survey highlight homebuyers' perception on how subjective factors influence housing markets. Its allows us to compare the perception of the influence of short-term factors on the market with the economic fundamental drivers of the economy."

Marguerite Simo
Senior Specialist, Housing research

Survey instrument

CMHC designed a survey to gain a better understanding of what motivates homebuyers and to understand how they structured their choices through the purchasing process. Specifically, the questionnaire zeroes in on how individuals relate to local market conditions during the purchase process, measures the degree to which social groups and external influences affect the perception of homebuyers' behaviours, measures homebuyers' expectations of future home prices, and finally, compares how homebuyers value alternative investment vehicles. In the 2018 edition of the survey, a few questions were added about attitude toward risk, to examine how respondents' risk tolerance interacts with housing decisions.

The questionnaire was mailed to 65,000 households who purchased a home in the Montréal, Toronto and Vancouver CMAs in the fall of 2018.

Respondents were invited to access the questionnaire via a secured website provided in the mail-out invitation. The response rate was the highest in Montréal, with 9% completed, followed by Vancouver, with 7%, and Toronto, with 5%. The survey is statistically representative of homebuyers in each CMA in 2018.⁷ This means the responses collected reflect the population as a whole, and the results presented below can be generalized to the populations of Vancouver, Toronto and Montréal.

We focused on expectations of price growth and on changes in those expectations. In addition, the key findings are as follows:

- A large majority of homebuyers think that fundamentals have less impact on house prices than factors linked to speculation. For instance, 27% of homebuyers in Montréal thought that employment growth has a lot of influence on house prices, while 52% of them thought that foreign investors have a lot of influence.
- Three quarters of the respondents indicated they were less willing to take financial risks. Respondents who participated in a bidding war did not have a higher tolerance for risk than respondents who did not participate in a bidding war.
- A high proportion of respondents (88%) thought that real estate is the best long-term investment, even better than financial investments.
- While the results of the questionnaire showed relatively little change between 2017 and 2018 in Vancouver and Toronto, respondents in Montréal reported spending more than they budgeted to a greater extent in 2018. A higher proportion of them also perceived that foreign investors have significant influence (52%, versus 42%).
- Price growth expectations in one year were quite similar to the actual price changes the year before, except in Montréal where price growth expectations in 2018 were lower than the actual changes in 2017.

Price growth expectations: homebuyers possibly form their expectations by looking into the past (backward-looking view)

Price growth expectations are the first subjective factor analyzed in this report. This section compares the past two years of survey results between actual price growth and price growth anticipated over the following year.

Table 1 shows actual house price changes from MLS® data for 2016 and 2017, with the average expectations as reported by homebuyers for 2017 and 2018.⁸ Price growth expectations in one year were quite similar to the actual price changes the year before, except in Montréal where price growth expectations in 2018 were lower than the actual changes in 2017.

The respondents' expectations were consistent with the actual changes in the previous 12 months, instead of the actual changes in the following 12 months, especially for respondents from Vancouver and Toronto. While

we cannot provide more substantial statistical evidence because of a lack of data, this may still suggest that respondents possibly form their expectations by looking into the past (backward-looking view) rather than looking forward.

In Vancouver, in particular, respondents had a more bearish outlook for the housing market for the following 12 months: price growth expectations went from 10% in 2017 to 1% in 2018. This can also be due to structural uncertainties in the global economy in 2018 that were not evident in 2017.

One could think that homebuyers involved in a bidding war would have higher price growth expectations and a higher appetite for risk than other homebuyers. In fact, there was no difference in house price expectations between homebuyers who were involved in bidding wars and homebuyers who were not. Homebuyers who were involved in bidding wars did not have higher price growth expectations nor a higher appetite for risk than the rest of homebuyers.

Finally, short-term expectations were very low in 2018, but a majority of respondents (88%) maintained the idea that real estate is the best long-term investment. This is consistent with some empirical results obtained in the United States, where short-term expectations were linked with the homebuying decisions of individuals.⁹

Homebuyers' financial risk perception

Financial risk perception is another subjective factor that can influence purchase behaviours and, ultimately, house prices. Our dataset enables us to analyze one main hypothesis. Homebuyers who are not willing to take financial risks are less likely to spend more than they budgeted compared to other homebuyers.

In this regard, this section analyzes the self-perceived financial risk profile of homebuyers. To that end, in this year's edition of the survey, we added a few questions about attitude toward risk.¹⁰ The intention was to gain better knowledge of financial risk perception among homebuyers.

Table 1: Price growth expectations over succeeding year versus actual price changes, with 10% trimmed data, all property types

	Actual change Sept. 2016 to Sept. 2017	Survey expectation 12-month (2017-2018) average	Actual change Sept. 2017 to Sept. 2018	Survey expectation 12-month (2018-2019) average
Vancouver	9%	10%	1%	1%
Toronto	4%	5%	4%	4%
Montréal	5%	4%	7%	3%

Sources: MLS®, Centris® and CMHC

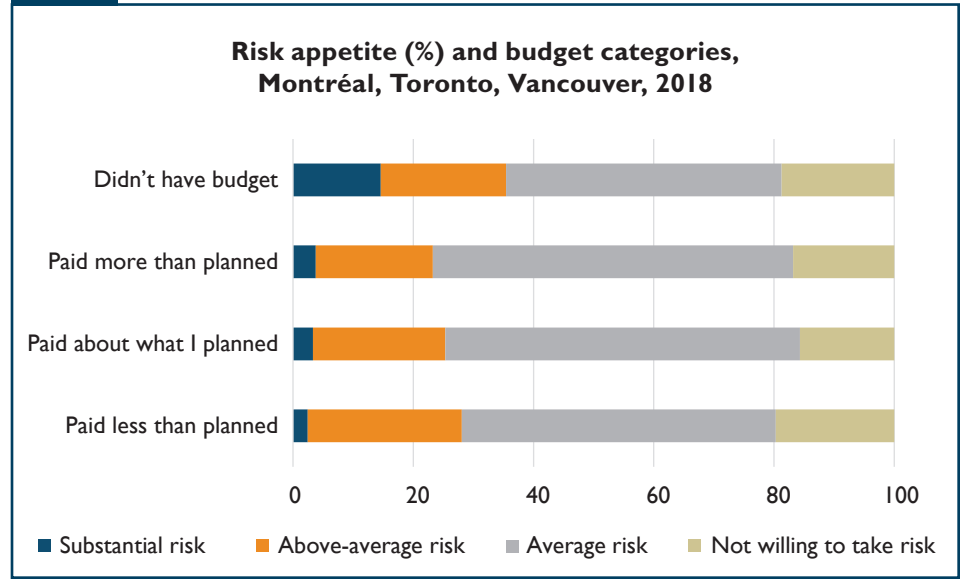
Perceived financial risk profile and budget

According to the respondents, a majority of homebuyers indicated they were less willing to take financial risks (75%). This result was consistent across the three markets (77% in Montréal, 72% in Toronto and 76% in Vancouver).

Contrary to our hypothesis, figure 1 shows that homebuyers who indicated they were less willing to take financial risks were not less likely to spend more than they budgeted compared to the rest of homebuyers. Instead, the proportions of the two groups were quite similar for the “Paid more than planned” category (19% and 60%) and the “Paid about what I planned” category (22% and 59%).

At one end of the spectrum, homebuyers who were not willing to take any financial risks were the ones with the highest proportion of those who paid less than they planned. At the other end, homebuyers who were willing to take substantial risks were the ones with the highest proportion of those who did not have any budget. Homebuyers who were not willing to take any financial risks purchased houses with the lowest values. This was true for each market and overall, for all risk and housing types.

Figure 1



Source: CMHC, Home Buyer Motivation Survey, 2018

Age and income of homebuyers influence their propensity to take financial risks

The goal of this section is to analyze whether income level, age and buyer status have an impact on the self-declared risk profile.

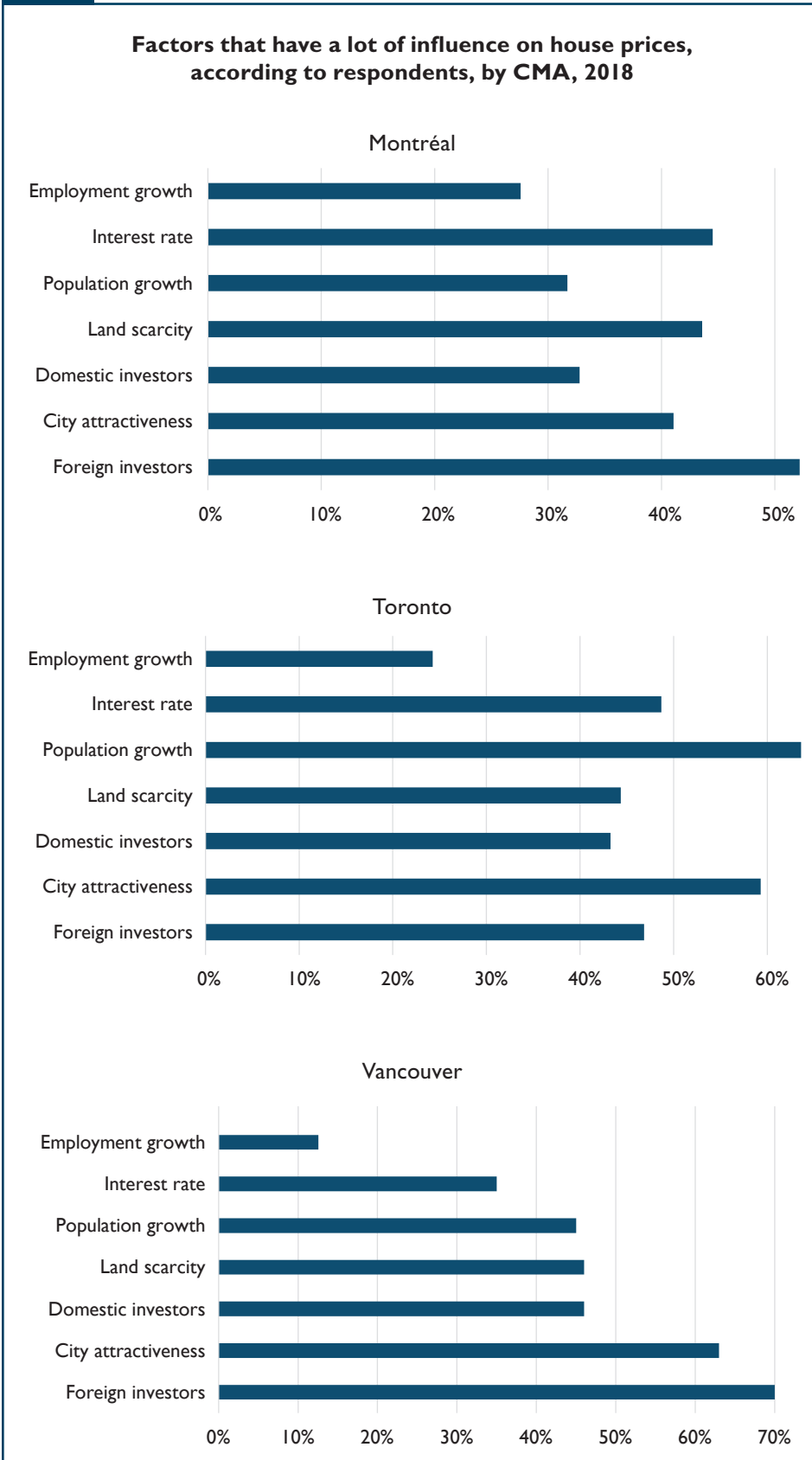
The data analysis reveals that financial risk appetite decreases with the age of homebuyers. Among young buyers under the age of 35, 88% had some appetite for financial risk. This is consistent with many empirical studies presented in the behavioural economics literature.¹¹ In addition, the higher the income of

respondents, the more willing they are to take financial risks. Indeed, 31% of the respondents who were not willing to take risks earned less than \$60,000, while only 11% of those who were not willing to take risks earned more than \$200,000.

Finally, there was no significant difference between first-time homebuyers and repeat homebuyers, and the risk profiles were the same among first-time homebuyers and repeat homebuyers.

In conclusion, older homebuyers with higher incomes are more willing to take financial risks than the rest of homebuyers in general.¹²

Figure 2



Factors linked to speculation influencing home prices

Fundamentals drivers (interest rate changes, employment growth, population growth) are thought by homebuyers as having less impact on house prices than factors linked to speculation, (foreign buyers, domestic investors, city attractiveness) (figure 2). Respondents' perceived traditional fundamental drivers, such as employment growth, interest rate changes and population growth, to be less influential than subjective ones linked to speculation, such as city attractiveness and the presence of foreign investors. The dominance of short-term factors was obvious in Vancouver, while respondents in Toronto perceived population growth to be influencing housing prices the most. The fact that short-term factors have a greater influence on house prices can lead to higher house price growth expectations that in turn makes homebuyers more willing to pay a higher price for homes.

Another interesting finding was that there was a change in the perception of homebuyers in Montréal regarding the impact of foreign investors. In 2018, the perception of foreign investors influencing home prices rose to 89%, from 81% in 2017. Additionally, the proportion of homebuyers in Montréal who perceived foreign investors as having a lot of influence on house prices rose from 42% to 52%.

The lack of a foreign buyers' tax in the Montréal market could be one of the many reasons behind this Montréal-only phenomenon. However, there is no hard data to prove this point.

Source: CMHC, Home Buyer Motivation Survey, 2018

Overview of purchase behaviours

In this section, we report descriptive statistics comparing bidding wars with some of the results from the report published in 2017. We also hone in on some of the changes observed in the Montréal market.

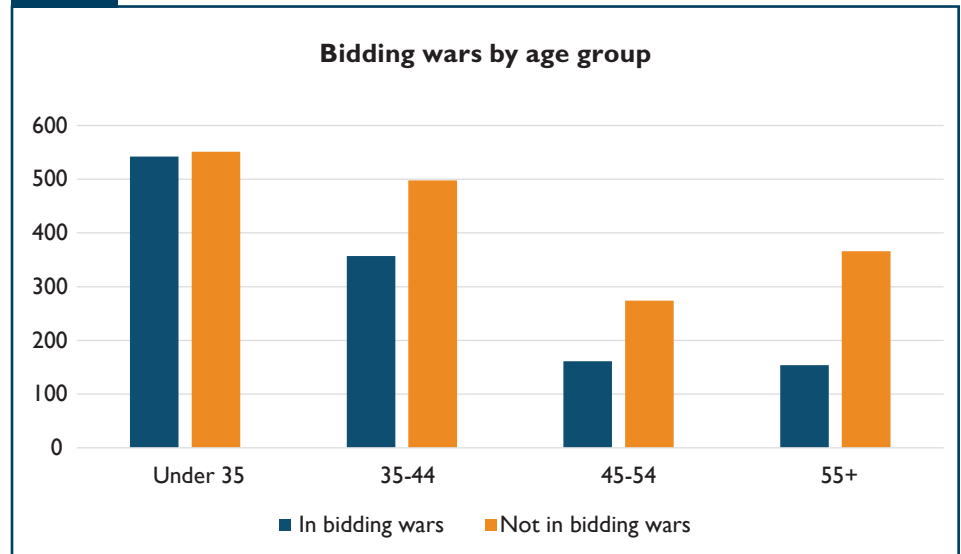
Bidding wars

The proportion of homebuyers who experienced a bidding war in Toronto declined from 55% to 45% between 2017 and 2018. Meanwhile, the proportions remained the same in Vancouver (55%) and Montréal (24%).

Figure 3 shows that nearly half of the respondents participated in a bidding war. Overall, premium amounts decreased between 2017 and 2018. In 2018, homebuyers involved in bidding wars spent 24% more than the median price. In 2017, the premium was 45% more than the median. More specifically, the premiums, in median terms, were 18% for single-detached houses and 15% for condominiums and apartments.

Given the small number of observations, results cannot be provided by CMA. Nevertheless, some interesting facts were noted in some markets. In Vancouver, for single-detached houses, more than 45% of the bidding wars occurred for houses with prices lower than the 10th percentile. This illustrates the difficulty of entering the single-detached home market in Vancouver. Conversely, in Montréal's condominium market, there was a relatively high occurrence of bidding wars for homes with prices above the 90th percentile (14%). This could suggest a higher demand for high-end condominiums in Montréal.

Figure 3



Source: CMHC, Home Buyer Motivation Survey, 2018

Table 2: Income growth and average growth in nominal and real house prices

	Montréal	Toronto	Vancouver
	% (from 2017 to 2018)		
Real income growth per capita	3.5	-1	-1.5
Young adult population growth	1.5	3.7	1.1
Average growth rate in nominal house prices	6.6	3.4	0.5
Average growth rate in real house price	4.3	0.8	-1.9

Sources: MLS®, Centris® and Conference Board of Canada

Montréal market accelerates

Evidence shows that the Montréal market is heating up this year. According to MLS® and Centris® data, between 2017 and 2018, the Montréal CMA recorded higher house price growth than Toronto or Vancouver. The changes in actual MLS® house prices were less than 0.66% in Vancouver and 3.65% in Toronto but 6.57% in Montréal.

As discussed in CMHC's *Housing Market Assessment*,¹³ demand fundamentals in Montréal were strong in 2018. Table 2 shows that

income growth in the Montréal CMA outpaced the growth in the Toronto and Vancouver CMAs, and young adult population growth in Montréal outpaced that in Vancouver but not that in Toronto. This shows that higher house price growth in the Montréal market is supported by higher demand fundamentals growth.

The results of the survey are in line with these data. For instance, more people spent more than budgeted in Montréal (from 24% in 2017 to 28% in 2018). During the same time, the proportions remained stable in Vancouver (49%) and Toronto (48%).

METHODOLOGY FOR HOMEBUYERS' MOTIVATIONS SURVEY

CMHC conducts the Homebuyers' Motivations Survey to facilitate quantitative research on behaviours of recent homebuyers, in order to determine the impact of their perceptions and motivations on housing prices. This large-scale survey targets consumers who recently purchased a residential property in the Toronto, Montréal and Vancouver CMAs and has two intended purposes:

- collect data on homebuyer behaviours and influential factors involved in their purchasing decisions; and
- support in-depth statistical analysis on how well homebuyers understand the housing market and whether their behaviours reflect long-term characteristics of the housing market; CMHC selects a random sample of approximately 10,000 residential properties that were sold within the previous 12 months in each of the three target CMAs.

The information is collected using a questionnaire developed by CMHC. The questionnaire contains about 35 questions, including mostly multiple-choice questions, rating-scale questions and fill-in-the-blank questions. A mix of online questionnaires and computer-assisted telephone interviews (CATIs) is used to collect the data. The collection period is from mid-September to mid-October.

ENDNOTES

- ¹ In this analysis, we consider homebuyers who are less willing to take financial risks to be the ones who gave this response to the survey: "I take average financial risks expecting to earn average returns," or "I am not willing to take any financial risks."
- ² In this article, we consider employment growth, interest rate, population growth and land scarcity as fundamental factors while domestic investors and foreign investors are regarded as factors linked to speculation.
- ³ Canada Mortgage and Housing Corporation (2018). *Examining Escalating House Prices in Large Canadian Metropolitan Centres*.
- ⁴ Bailey M., E. Davila, T. Kuchler and J. Stroebel (2018). "House Price Beliefs and Mortgage Leverage Choice," *The Review of Economic Studies*, rdy068, <https://doi.org/10.1093/restud/rdy068>.
- ⁵ Zwick E., C. Nathanson and A. DeFusco (2017). "Speculative Dynamics of Prices and Volume," NBER, Working Paper 23449.
- ⁶ Canada Mortgage and Housing Corporation (2018). *Housing Market Insight—Canada*, June 2018.
- ⁷ In the survey, we look at specific components of homebuyers such as age, income and first-time homebuyer status, and we assume that these characteristics are homogeneous across the entire population.
- ⁸ The percentage change or growth in price is calculated by dividing the price of the current year by the price of the base year and then subtracting 1.
- ⁹ Adelino M., A. Schoar and F. Severino (2018). "Perception of House Price Risk and Homeownership," NBER, Working Paper 25090.
- ¹⁰ The respondents are required to choose one that best describes their appetite for risk from the follow options:
1. I take substantial financial risks expecting to earn substantial returns
2. I take above average financial risks expecting to earn above-average returns
3. I take average financial risks expecting to earn average returns
4. I am not willing to take any financial risks.
- ¹¹ Albert S. and J. Duffy (2012). "Differences in Risk Aversion between Young and Older Adults," *Neuroscience and Neuroeconomics*, Vol. 1.
- ¹² This conclusion is generalized by looking into both factors together as older homebuyers tend to have higher income at the same time whereas if we look at the age alone, risk appetite decreases with the age of homebuyers.
- ¹³ Canada Mortgage and Housing Corporation (2019). *Housing Market Assessment—Canada*, First Quarter 2019.

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