

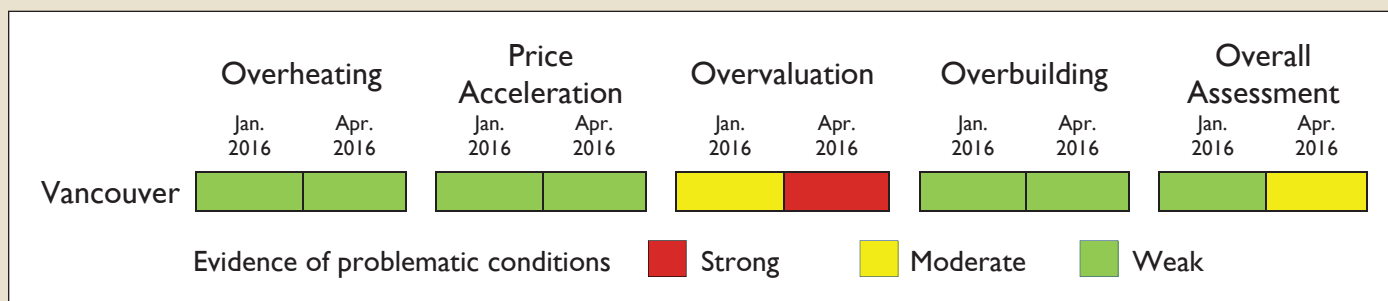
# HOUSING MARKET ASSESSMENT Vancouver CMA

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## Highlights



- Overall, we detect moderate evidence of problematic conditions<sup>1</sup> for the Vancouver Census Metropolitan Area (CMA) housing market in the fourth quarter of 2015, a change from the previous quarter when overall conditions suggested weak evidence of problematic conditions.
- The change in our overall assessment from the previous quarter was mainly influenced by a shift from moderate to strong evidence of overvaluation, indicating that home prices are above the level supported by economic and demographic fundamentals.
- The remaining indicators assessed continue to suggest weak evidence of problematic conditions.
- 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 Overview<sup>2</sup>

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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<sup>1</sup> Results are based on data as of the end of December 2015 and local market intelligence up to end of March 2016. CMHC continuously monitors market developments and will issue HMA updates on a quarterly basis.

<sup>2</sup> A detailed description of the framework is available in the appendix of the [National edition](#).

## In Detail

### Weak Evidence of Overheating

We detect weak evidence of overheating for the Vancouver CMA housing market. Although the sales-to-new listings ratio (a proxy for housing demand and supply) has been firmly in sellers' market territory (sales-to-new listings ratio of 45 – 60%) since late 2013, this indicator remains below the HMA threshold for overheating (Figure 1). The ratio has been trending up since the second quarter of 2014, indicating that home buyer demand has outpaced the supply of resale homes. Indeed, while fourth quarter 2015 MLS<sup>3</sup> sales were up

30 per cent compared to the same period a year earlier, the number of new listings increased by less than two per cent. Demand for all home types (single detached, town house and apartment) has been strong across the municipalities of the Vancouver CMA, with sales rising more steeply in some suburban areas than in the City of Vancouver<sup>4</sup>. Fourth quarter 2015 sales in New Westminster, Maple Ridge and Burnaby increased by 40 per cent or more, whereas sales in the City of Vancouver rose 17 per cent.

### Weak Evidence of Price Acceleration

Sustained seller's market conditions have put upward pressure on prices in the Vancouver CMA, however we detect weak evidence of a problematic

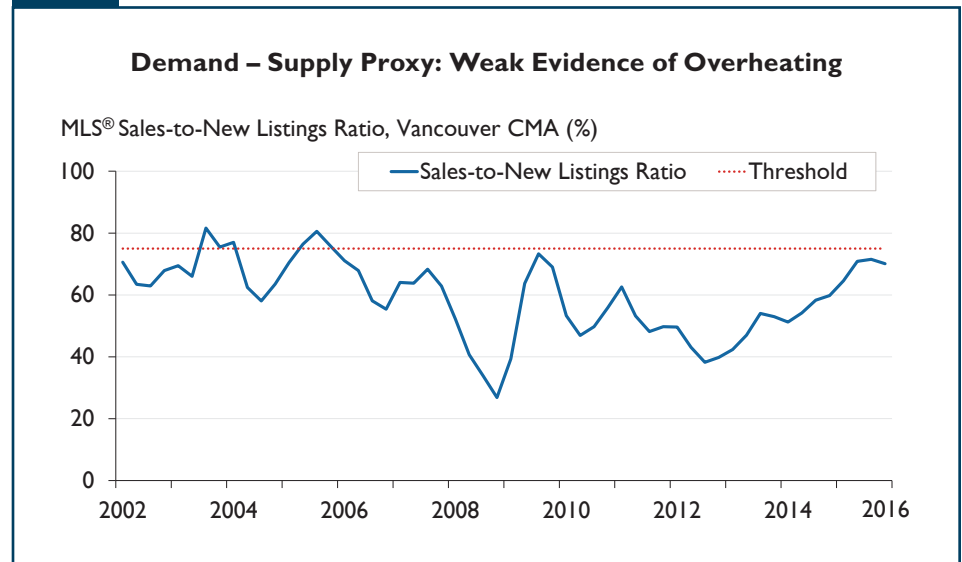
rate of price acceleration. The MLS HPI benchmark price<sup>5</sup> has been increasing in both the Fraser Valley and Greater Vancouver Real Estate Board areas since late 2013, however the pace of year-over-year (Y-O-Y) increase has been uneven, with detached home prices rising faster and for a longer period of time than apartment and town house prices (Figure 2). In the fourth quarter of 2015, detached home prices grew at their fastest rate, surpassing the previous peak pace of growth in 2006, while multi-family home prices have not surpassed previous peak rates of growth. The pick-up in the pace of multi-family (town houses and apartment condominiums) home price growth lagged behind that of single detached home price growth.

*“Overall, we detect moderate evidence of problematic conditions in the fourth quarter for the Metro Vancouver housing market, a change from weak evidence in the previous quarter. This change was due to a shift from moderate to strong evidence of home price overvaluation.”*



**Robyn Adamache**  
Principal, Market Analysis (Vancouver)

Figure 1



Sources: Real Estate Board of Greater Vancouver and Fraser Valley Real Estate Board, calculations (threshold) by CMHC. Last data point: 2015 Q4. MLS is a registered trademark of the Canadian Real Estate Association.

<sup>3</sup> MLS is a registered trademark of the Canadian Real Estate Association (CREA).

<sup>4</sup> Source: Real Estate Board of Greater Vancouver.

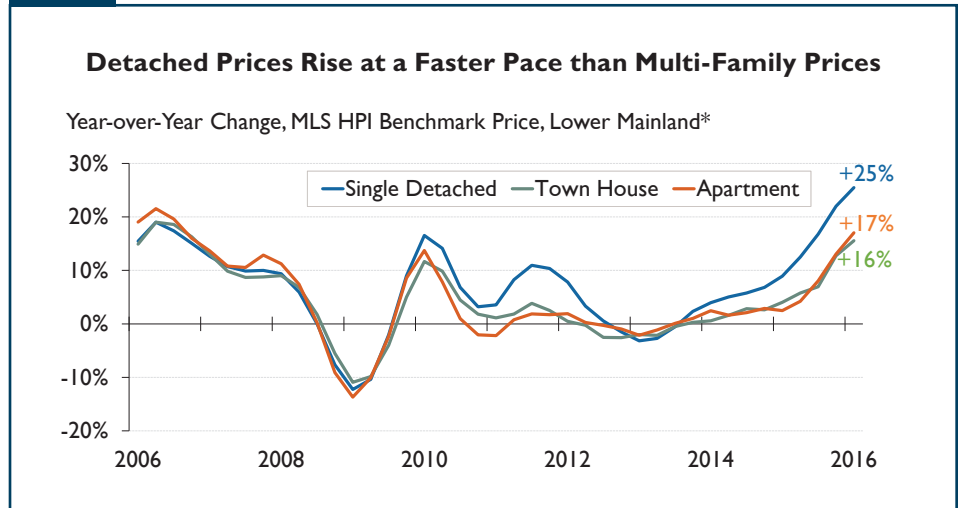
<sup>5</sup> This measure tracks the price of homes with common features, and is therefore is not subject to the limitations of average prices which can be skewed by prices on the low or high end of the spectrum. In markets like Vancouver, where the range in prices by area and by type is very wide, average prices can give a misleading view of overall conditions.

## Strong Evidence of Overvaluation

The fourth quarter 2015 HMA framework points to strong evidence of overvaluation of Vancouver CMA home prices, a shift from the previous quarter's assessment of moderate evidence. This indicates that the observed level of home prices is higher than the level warranted by underlying economic and demographic fundamentals. It is the first time we assess strong evidence of overvaluation in Vancouver despite robust and sustained house price increases since 2012 as housing demand fundamentals have been particularly robust in the region. The population has grown, adding an average of more than 15,000 new households per year over the last five years<sup>6</sup> and a diversified economy has led the province in job creation. Employment growth picked up in the first quarter of 2016, which should help bring underlying fundamentals more in line with home prices.

Strong demand for housing coupled with a limited supply of land for new development have combined to push home prices higher. While detached home prices have shown the strongest price response to these factors, multi-family home prices have also moved higher. The region's geographical restrictions on land supply<sup>7</sup> and the resulting high cost of land mean that most detached homes constructed in centres such as the City of Vancouver, Burnaby and North Vancouver add new supply through rezoning or infill, which has resulted in upward pressure on prices. In order to maximize the return on investment

Figure 2



Sources: CREA, calculations by CMHC

Last data point: 2016 Q1

\* Lower Mainland includes all centres of the Fraser Valley Real Estate Board and the Real Estate Board of Greater Vancouver (Including the Vancouver CMA and the Abbotsford-Mission CMA)

in an environment of high land costs, particularly in central locale that are zoned only for single-detached homes, developers are building larger new detached homes, often incorporating one or more secondary suites and/or a laneway homes. As a result, detached home prices have moved up and in turn impacted aggregate price measures.

A shift in the price distribution of sales has also contributed to higher average prices. Overall, 27 per cent of the homes sold in the fourth quarter of 2015 were over \$1 million compared to 19 per cent in the fourth quarter 2014.

While Vancouver CMA home prices are high, there is a range of housing available to buyers across a wide price spectrum. Prices vary widely by area and by home type, segmenting the market. Figure 3 illustrates the wide range in prices, with the top

quintile of all homes sold in the fourth quarter averaging \$2.15 million. When this group is removed from the data, the aggregate average price declines by more than \$300,000 to \$548,000. The upper quintile comprises mostly single-detached homes. High net worth individuals and those who have gained equity in their homes from sustained price growth in the region are engaged in this market, while the majority of other buyers focus on lower priced homes in condominium developments and suburban locations.

Low mortgage rates have aided affordability by keeping monthly mortgage payments relatively stable over time in inflation-adjusted terms. However, the down payment remains a challenge for first-time home buyers and repeat buyers with little equity in their home as continued home price appreciation drives down payment levels higher.

<sup>6</sup> Source: BC Stats P.E.O.P.L.E. 2015 Household projections, CMHC growth calculations.

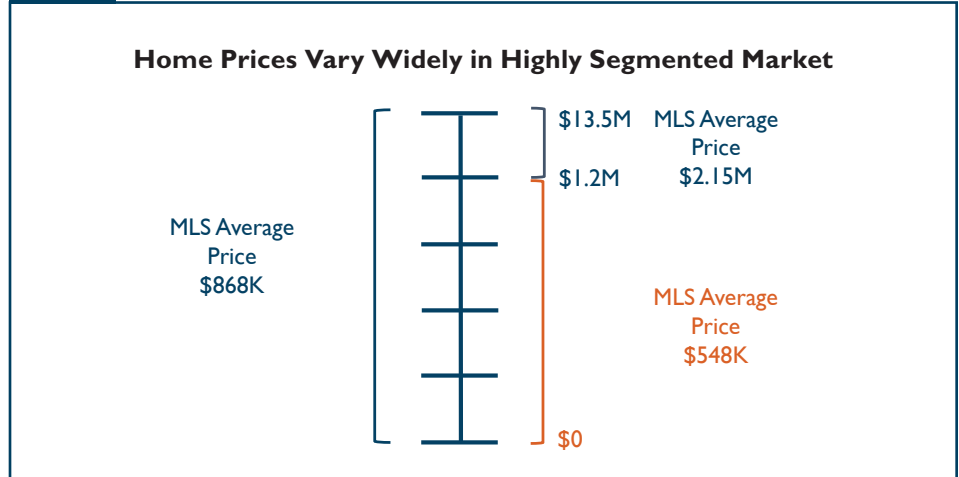
<sup>7</sup> Mountains to the north, the Strait of Georgia to the west, the U.S. border to the south and 22 per cent of the region's land supply dedicated to the Agricultural Land Reserve (ALR).

## Weak Evidence of Overbuilding

Evidence of overbuilding in the Vancouver CMA housing market remains weak according to the HMA. Demand for both resale and new homes has outpaced the available supply. The stock of active MLS® listings is declining as new listings are quickly purchased. In addition to buyers with a preference for new homes, those who are not able to find the right home on the resale market add to demand for new homes. As a result, the number of newly completed and unsold homes has been trending down for all home types since the first quarter of 2013 (Figure 4). To meet this demand, developers are bringing on more supply, with fourth quarter 2015 housing starts up 23 per cent compared to the same quarter of the previous year. Due to limited land supply and the resulting escalation in the cost of land, nearly 80 per cent of new homes started are multiple-family (town home and apartment) units, which satisfy demand for homes at the lower end of the price spectrum. However, it is difficult to respond quickly to demand for multi-family homes with large-scale complex condo projects, due to approval and construction processes that can take years to complete.

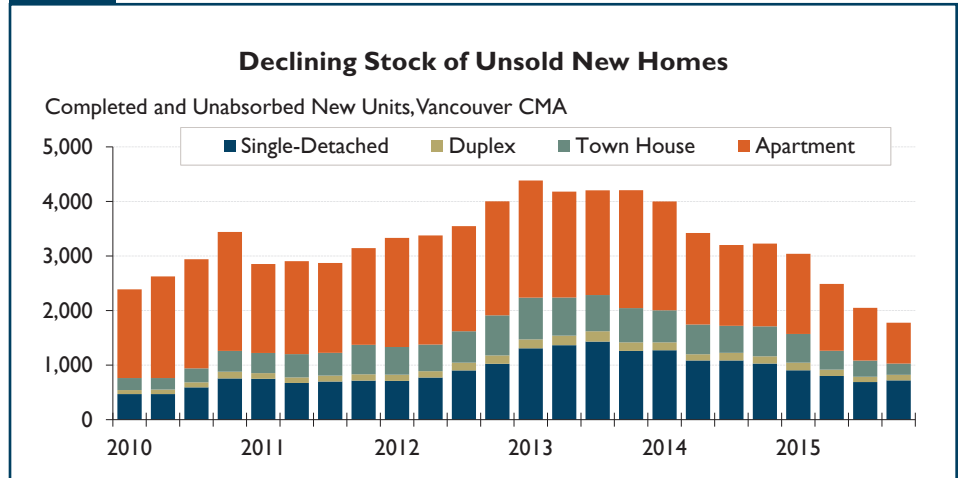
Sustained low rental vacancy rates in the Metro Vancouver region also contribute to the assessment of weak evidence of overbuilding. Robust demand for rental accommodation has kept the vacancy rate for both purpose-built and secondary rental apartments at or below one per cent since 2014<sup>8</sup>. Almost all municipalities in the

Figure 3



Source: REBGV, FVREB, CMHC Calculations, Fourth Quarter, 2015, Includes all home types.

Figure 4



Source: CMHC

Vancouver CMA recorded lower vacancy rates in 2015 than in the previous year. Secondary rental units, such as investor-held condominium apartments, have added to the rental housing supply in the region, contributing 14,829 additional units over the past five years, compared to 2,488 purpose-built rental apartments added to the stock during the same period<sup>9</sup>.

<sup>8</sup> CMHC Rental Market Survey, Condominium Vacancy Survey.

<sup>9</sup> CMHC Rental Market Survey, Condominium Vacancy Survey.



## 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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