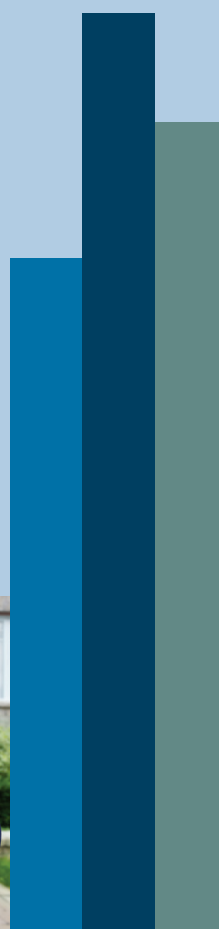


# HOUSING MARKET ASSESSMENT Ottawa<sup>1</sup>

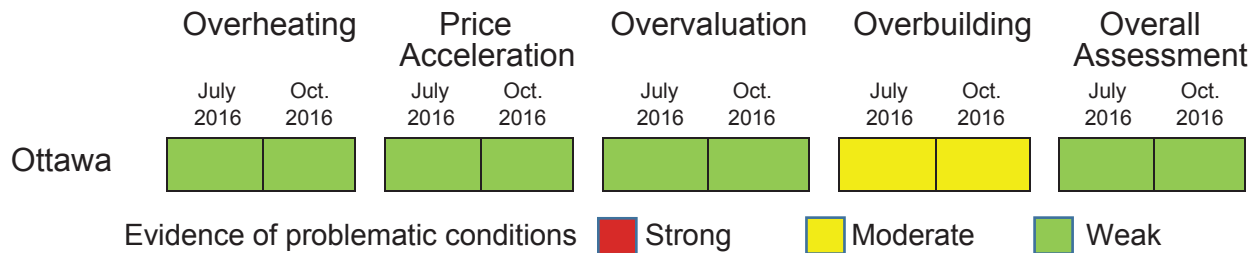
Date Released: Fourth Quarter 2016



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<sup>1</sup> Ontario part of Ottawa-Gatineau CMA

## Highlights



- The overall assessment for the Ottawa CMA is weak evidence of problematic housing market conditions.<sup>2</sup>
- We detect moderate evidence of overbuilding due to a high inventory of completed and unsold condominium<sup>3</sup> units, as well as a rise in vacancy rates as per the latest 2015 CMHC Rental Market Survey.
- We detect weak evidence of overvaluation as some price indices point to modest growth in prices, while other indices have posted declines.
- 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>4</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.

Color 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.

<sup>2</sup> Results are based on data as of the end of June 2016 and local market intelligence as of the end of September 2016. CMHC continuously monitors market developments and will issue HMA updates on a quarterly basis.

<sup>3</sup> Unless otherwise specified, condominiums or condominium units refer to condo apartments and condo rows. Condominium apartments make up about 99 per cent of total condominium starts on the new home market since 2010. On the resale market however, over the same period, condominium apartments made up around 50 per cent of total condominium transactions, while condo rows took up 35 per cent and the remaining share was taken up by stacked townhouse condos. Total condominium sales represent on average 20 per cent of all resale market activity.

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

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

## In Detail

### Overheating

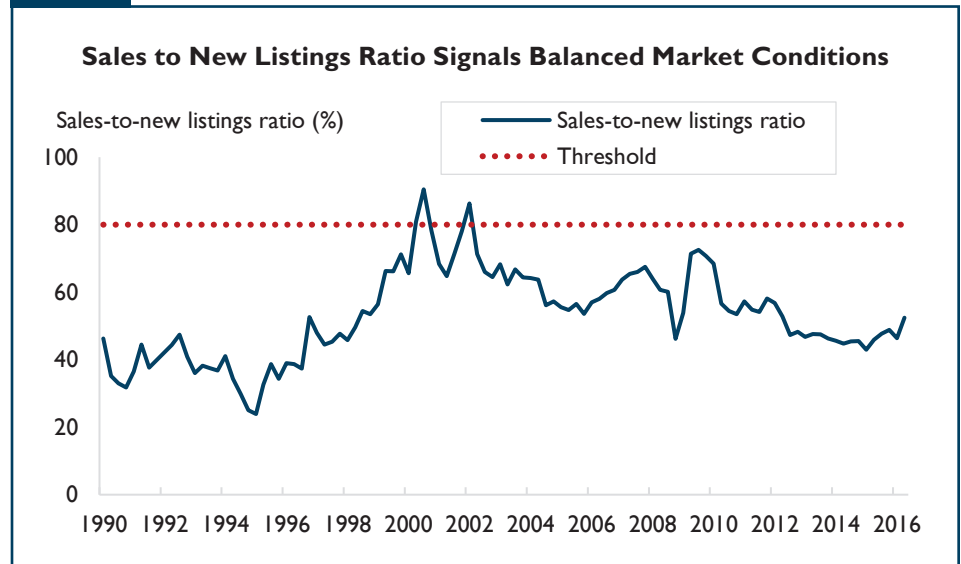
We detect weak evidence of overheating in the existing home market in the Ottawa CMA. Balanced<sup>5</sup> market conditions have prevailed in the resale market from Q2-2010 until present. In Q2-2016 the seasonally adjusted sales-to-new-listings (SNL) ratio went up to 52.5 per cent from 46 per cent in the previous quarter, substantially below the overheating threshold at 80 per cent or higher, whereby demand would be running far ahead of supply. Conditions in the resale market were once again segmented as activity on the freehold<sup>6</sup> and condominium sides of the market differed. For five out of the last six quarters, activity on the freehold side was in balanced market territory, while the condominium market was a buyers' market or at the edge of a

*"We detect moderate evidence of overbuilding in Ottawa due to a high inventory of completed and unsold condo units relative to the population."*



Anne-Marie M Shaker  
Senior Market Analyst

Figure 1



Sources: CREA, and calculations (threshold) by CMHC  
Last data point: Q2-2016

buyers' market in all but Q4-2015. In Q2-2016 the SNL ratio for freehold and condominium activity was at 56 per cent and 39 per cent, respectively. While overall market conditions remained in balanced territory, more recent data to August is showing a shift in trend toward balanced market conditions on the condominium side and sellers' market conditions on the freehold side.

### Price Acceleration

We detect weak evidence of price acceleration in the Ottawa market. Price growth has been around the rate of inflation over the 2013-2015 period due to soft demand conditions, as sales declined in 2013, saw flat growth in 2014, but rebounded in 2015. Although sales rose in Q2-2016, it was mostly due to a rise in single-detached and row home sales. Price growth was also supported by a rise in single-detached home prices, specifically

bungalows saw the strongest growth. In Q2-2016, condo apartment and condo row prices also grew following a decline in Q1-2016. The overall seasonally adjusted average MLS<sup>®</sup> price was trending at an annualized rate of 1.5 per cent in Q2-2016, but the price was down 0.8 per cent from the same quarter last year. The most recent data in August point to a minor upward trend in the CREA MLS<sup>®</sup> HPI Benchmark Price.

### Overvaluation

We detect weak evidence of overvaluation for the Ottawa CMA, with average overvaluation hovering just below the problematic threshold. While, Ottawa had witnessed strong price growth at intermittent times during the last decade, recent years have seen growth rates moderate considerably. In Q2-2016 the seasonally adjusted average MLS<sup>®</sup> price grew a modest 0.38 per cent compared to Q1-2016, while

<sup>5</sup> Balanced market bounds are 40 to 60 per cent. Lower than 40 per cent, the ratio implies a buyer's market; 60 to 80 per cent implies a seller's market, 80 per cent and above implies overheating.

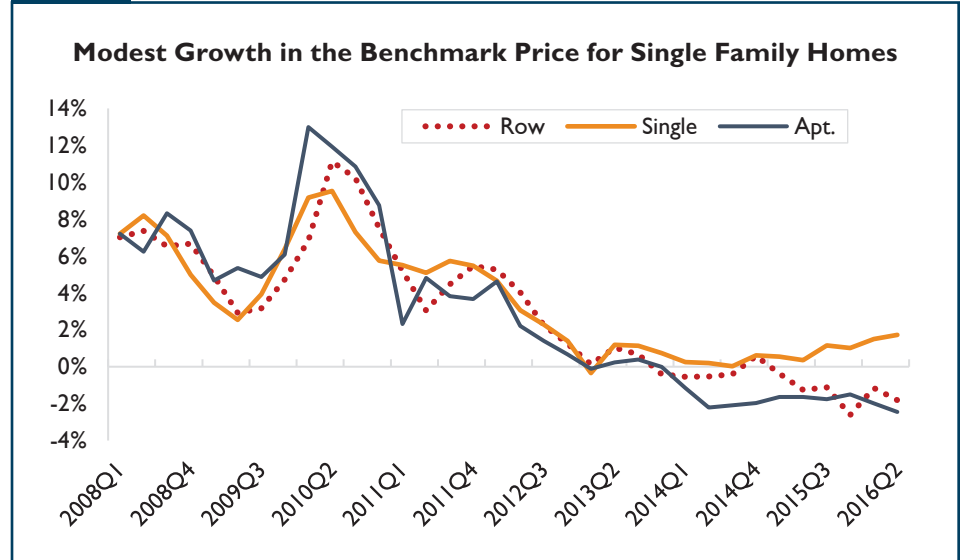
<sup>6</sup> Freeholds include homeowner single-detached homes, semis and rows.

seasonally adjusted earnings<sup>7</sup> grew at a much stronger rate of 2.2 per cent, providing evidence for dissipating overvaluation. Employment has been trending up from the end of last year and grew 1.5 per cent in Q2-2016 compared to the previous quarter. Year-to-date to August, employment continued on an upward trajectory.

## Overbuilding

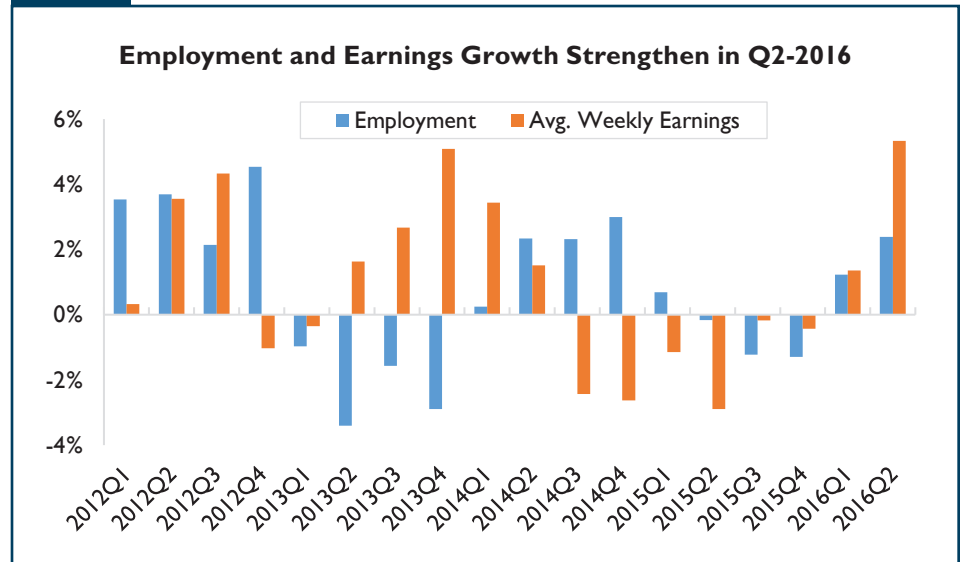
We detect moderate evidence of overbuilding for Ottawa. The condominium apartment construction boom that took place between 2012 and 2013 led to rising completions from 2014 to 2015. The number of newly completed and unsold units (homeowner and condo) per 10,000 population had hit an all-time high in February 2016, and although the number has declined since, it still remains elevated. The number of unsold units has come down in August, as improved employment conditions in Q2-2016 supported demand in the resale and new home market. In addition, the seasonally adjusted number of condominium apartment units under construction has been steadily trending down since peaking at 3,653 units in December 2013, and is currently at 1,196 units in August. However, inventory management continues to be necessary until the high number of completed and unsold units are absorbed by the market. A rise in the vacancy rate<sup>8</sup> for both purpose-built apartment units and condominium apartment units offered for rent is also contributing to the detection of moderate evidence of overbuilding in Ottawa. Additional supply to the market is also coming from the rental apartment side. Another 436 rental

Figure 2



Sources: CREA, growth calculations by CMHC  
Last data point: Q2-2016

Figure 3



Sources: Statistics Canada, and year-over-year growth calculations by CMHC  
Last data point: Q2-2016

apartment units were added from July 2015 to June<sup>9</sup> 2016, 35 per cent lower than the previous year, but 24 per cent higher than the five-year

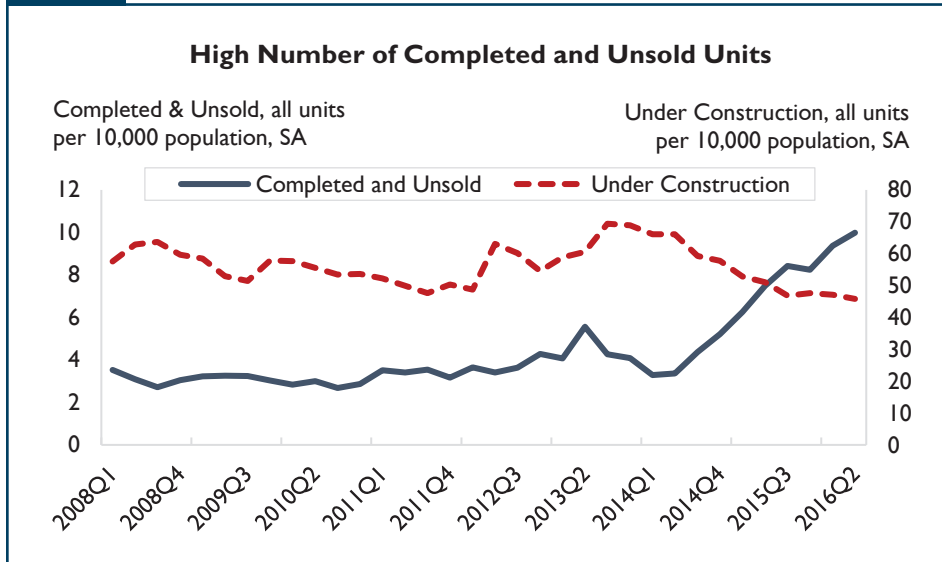
average. The rise in completed and unsold condominium apartment units is the primary driving force causing the rise in overall unsold units.

<sup>7</sup> Average weekly earnings are used here as a proxy for income.

<sup>8</sup> Available information on the vacancy rate for purpose-built apartments and condominium apartments offered for rent comes from the latest CMHC Rental Market Report conducted in October 2015. The purpose-built apartment vacancy rate had risen to 3.4 per cent from 2.6 the previous year, while the vacancy rate for condominium apartment units also went up to 2.6 per cent from 1.7 per cent.

<sup>9</sup> New rental completions to June 30th of each year are included in the CMHC October Rental Market Survey.

Figure 4



Source: Statistics Canada and CMHC, seasonal adjustment and calculations by CMHC.  
 Last data point: Q2-2016

## 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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