

HOUSING MARKET ASSESSMENT

Ottawa¹

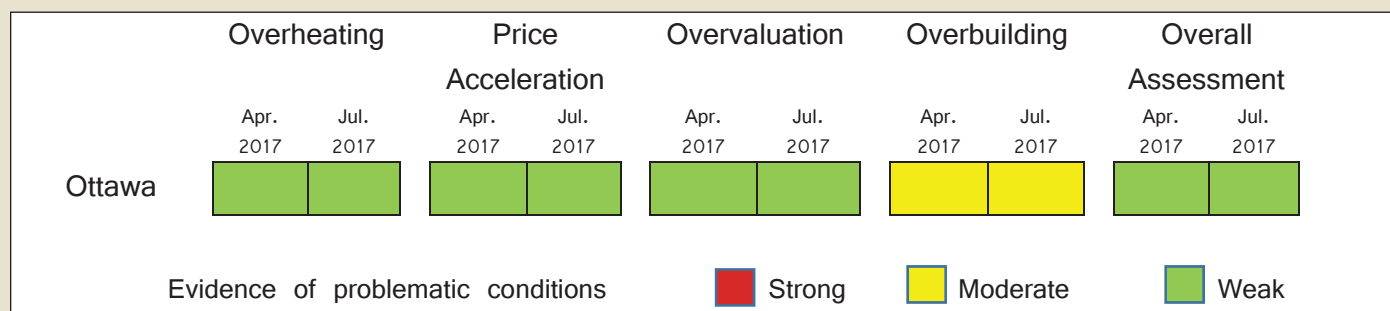
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Housing market intelligence you can count on

¹ Ontario part of Ottawa-Gatineau CMA

Highlights



- The overall assessment for the Ottawa CMA is weak evidence of problematic housing market conditions.²
- We detect moderate evidence of overbuilding due to a high but declining inventory of completed and unsold condominium³ units.
- We detect weak evidence of overvaluation as price indices point to a modest upward trend in prices.
- 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 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 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. As the number of intense and persistent signals increases, the associated evidence of problematic conditions becomes stronger.

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² Results are based on data as of the end of March 2017 and local market intelligence as of the end of June 2017. CMHC continuously monitors market developments and will issue HMA updates on a quarterly basis.

³ Unless otherwise specified, condominiums or condominium units refer to condominium apartments and condominium rows. Condominium apartments make up about 99% 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% of total condominium transactions, while condo rows took up 35% and the remaining share was taken up by stacked townhouse condos. Total condominium sales represent on average 20% of all resale market activity.

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

In Detail

Overheating

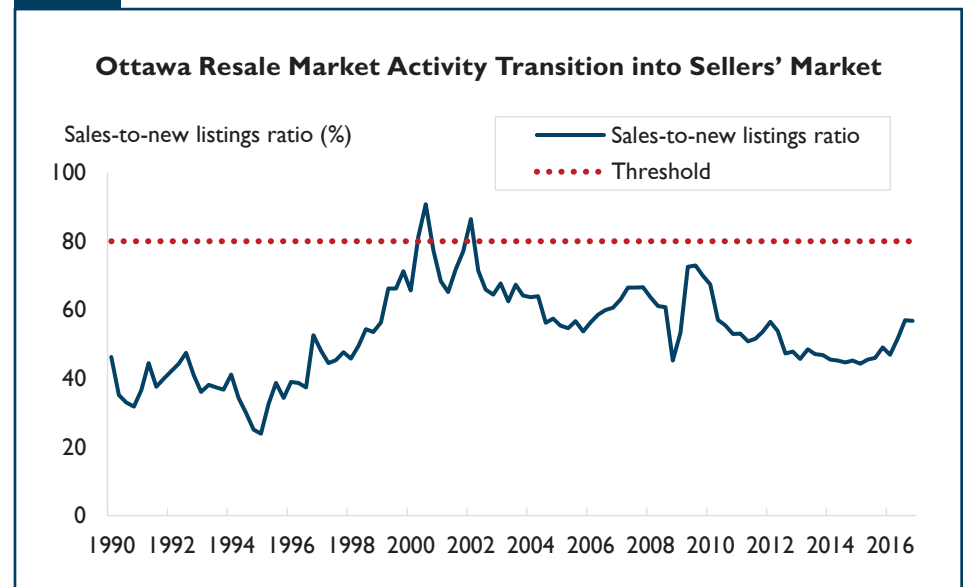
We continue to detect weak evidence of overheating in the existing home market in the Ottawa CMA. As of the third quarter in 2016, resale market activity had been trending quite close to the higher bound of a balanced⁵ market. In Q1-2017, with a seasonally adjusted sales-to-new-listings (SNL) ratio roughly around 61%, market conditions shifted to a sellers' market for the first time since Q2-2010. However, the SNL ratio remains substantially below the overheating threshold of 80%, whereby demand would be running far ahead of supply. The tilt toward sellers' market conditions in Q1-2017 was driven by stronger sales on the freehold⁶ side of the market, while conditions on the condominium side of the market remained in balanced market territory. More recent seasonally adjusted data to June point to a further rise in the SNL ratio on the freehold side of the market,

and near sellers' for condominium activity. These prevailing sellers' market conditions indicated improved demand conditions on both sides of the market, following decreased condominium demand over the 2011-2014 period.

Price Acceleration

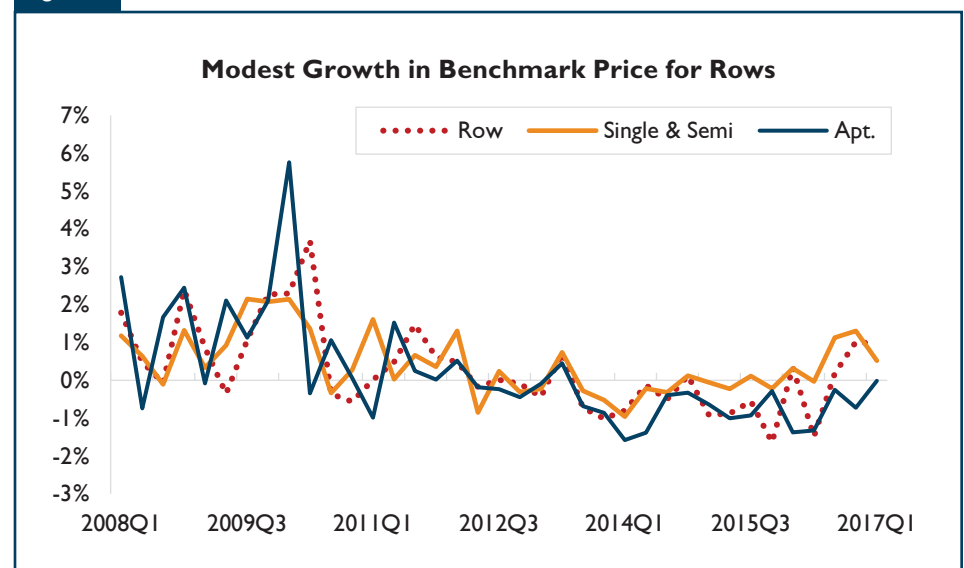
We detect weak evidence of price acceleration in the Ottawa market. Flat or declining condominium average prices coupled with modest growth on the freehold side kept

Figure 1



Sources: CREA, and calculations (threshold) by CMHC. Last data point: Q1-2017

Figure 2



Sources: CREA, seasonal adjustment, and quarter-over-quarter growth calculations by CMHC. Last data point: Q1-2017

"We detect moderate evidence of overbuilding in Ottawa due to a high inventory of completed and unsold condominium apartments relative to demographic indicators."



Anne-Marie M Shaker
Senior Market Analyst

⁵ Balanced market bounds are 40% to 60%. Lower than 40%, the ratio implies a buyer's market; 60% to 80% implies a seller's market, 80% and above implies overheating.

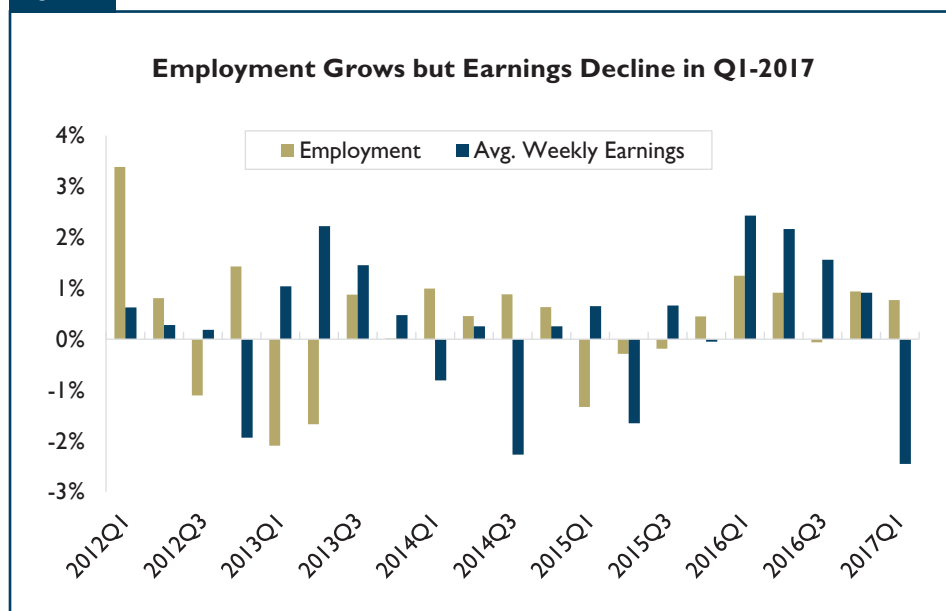
⁶ Freeholds include homeowner single-detached homes, semis and rows.

the overall MLS® annual average price growth below 2% from 2013 to 2016, and below the problematic threshold for price acceleration. However, the MLS® average price trended⁷ up significantly in Q4-2016, but growth moderated once more in Q1-2017. Nevertheless, year-over-year price growth hovered around 5% in Q4-2016 and Q1-2017, the strongest pace since Q3-2011. Looking at the CREA MLS HPI Benchmark⁸ seasonally adjusted quarterly price movements, Q1-2017 saw low-rise homes leading price growth, particularly rows as their sales grew at a stronger rate than singles this quarter, rebounding from a decline in Q4-2016. The sales-to-active-listings⁹ ratio for rows in Q1-2017 was 44%, relative to 22% for single-detached homes, and 17% for apartments signaling stronger market activity for rows. However, single-detached homes are still the most sought after dwelling type in Ottawa, making up over half the resale market transactions.

Overvaluation

We detect weak evidence of overvaluation for the Ottawa CMA, with average overvaluation below the problematic threshold. Adjusted for inflation, annual average price growth in Ottawa has been just below 1% over the 2012-2016 period, and declined in 2014. Real earnings¹⁰ growth also remained weak over most of the period, with the exception of 2016, when

Figure 3



Source: CMHC, adapted from Statistics Canada. Seasonal adjustment, and quarter-over-quarter growth calculations by CMHC
Last data point: Q1-2017

earnings had rebounded strongly, improving overall affordability. In Q1-2017, both real price and earnings declined compared to the previous quarter¹¹. Since price and earnings movements have been fairly aligned in Ottawa in recent years, the potential for overvaluation remains at bay. Meanwhile, employment continued to trend higher particularly in terms of full-time job growth, following an already strong showing last year, also supporting housing demand. Recent data to June point to stronger price growth, some weakening in employment but strengthening in earnings, albeit at modest rates.

Overbuilding

We detect moderate evidence of overbuilding for Ottawa. The number of completed and unsold dwelling units trended down for the third consecutive quarter, but remained substantial in absolute terms and relative to 10k population. The slow decline in inventory is driven by a decline in completed and unsold apartments (homeowner and condominium) which have represented on average 60% of total inventory since 2014, the year when inventory levels began to rise. Low-rise inventory has also been trending down since the end of 2016. Overall,

⁷ To compare quarterly price movements, the data is seasonally adjusted.

⁸ This is a trend measure of the change in home prices over time that takes into account the type of homes sold.

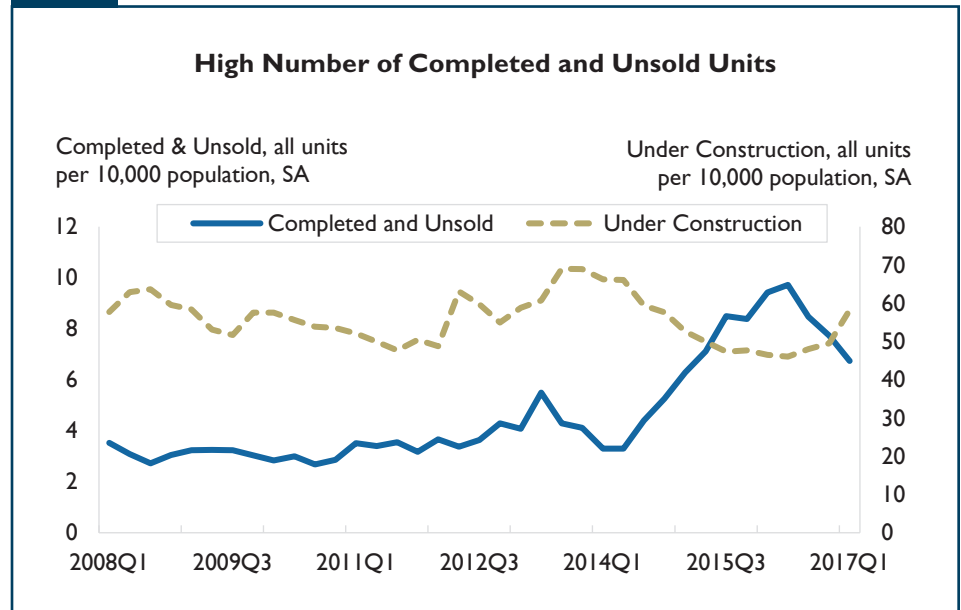
⁹ A sales-to-active-listings (SAL) ratio of less than 14% is a buyers' market, and greater than 20% is a sellers' market. The SAL statistic is available by dwelling type, while SNL statistic is only available for freehold and condominium transactions as a whole.

¹⁰ Average weekly earnings are used here as a proxy for income.

¹¹ Throughout the report, when comparing movements from one month to the next, or one quarter to the next, data are seasonally adjusted.

the number of unsold units reached 6.7 units per 10k population by the end of Q1-2017, while more recent data to June point to a minor uptick to 7.1 units per 10k population. Improved employment and earnings in 2016 have supported demand in the resale and new home markets.¹² The seasonally adjusted number of condominium apartment units under construction trended up once more to 2,098 units in Q1-2017, its highest level since Q2-2015, but remains below peak levels in previous years. Inventory management therefore continues to be necessary until the high number of completed and unsold units are absorbed by the market.

Figure 4



Source: Statistics Canada and CMHC, seasonal adjustment and calculations by CMHC.
Last data point: Q1-2017

¹² Seasonally adjusted condominium apartment sales grew a strong 12% in Q4-2016 on top of 13.9% growth in the previous quarter signaling improved demand conditions. For the year, condominium apartment sales grew 6.7% over 2015. The vacancy rate for both purpose-built and condominium apartment units offered for rent also eased in 2016 according to the latest CMHC Rental Market Report conducted in October 2016. The purpose-built apartment vacancy rate declined to 3.0% from 3.4 the previous year; while the vacancy rate for condominium apartment units also went down to 1.1% from 2.6%.

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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