

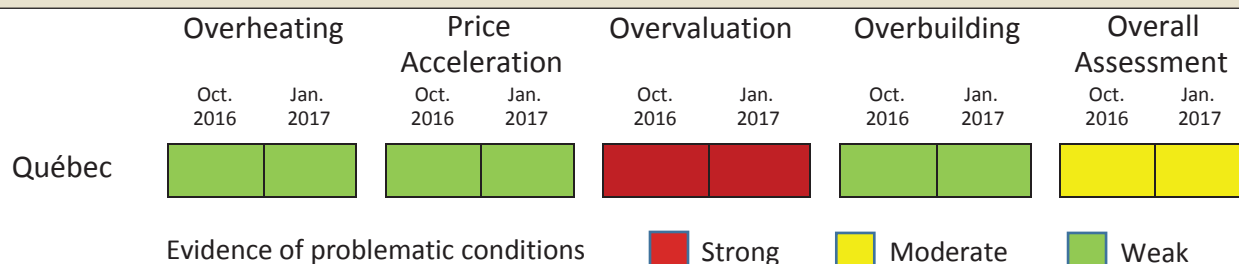
# HOUSING MARKET ASSESSMENT Québec CMA

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## Highlights



- Overall, the results from the Housing Market Assessment (HMA) still indicated moderate evidence of problematic conditions for the Québec census metropolitan area (CMA) in the third quarter of 2016<sup>1</sup>.
- While the signals have been tending to grow weaker since the beginning of 2016, there continued to be strong evidence of overvaluation. In fact, the HMA showed that house prices were above the levels warranted by underlying demographic and economic fundamentals.
- The HMA did not raise any concerns with regard to overheating or price growth acceleration. These results were attributable to the significant supply of properties, particularly condominiums, for sale on the existing home market.
- Evidence of overbuilding remained weak, but the situation should be monitored closely given the sustained level of conventional rental housing construction and the clear upward trend in the vacancy rate.
- 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 7 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 on account of 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 level of evidence of problematic conditions. The HMA is a comprehensive

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<sup>1</sup> Results are based on data as of the end of September 2016 and local market intelligence up to the end of December 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](#).

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.

## In Detail

### Overheating

According to the analytical framework, evidence of overheating in the Québec CMA remained weak in the third quarter of 2016. In fact, the sales-to-new listings ratio (SNLR), at about 48 per cent, stayed well below the problematic threshold of 70 per cent. The level of supply in relation to demand on the resale

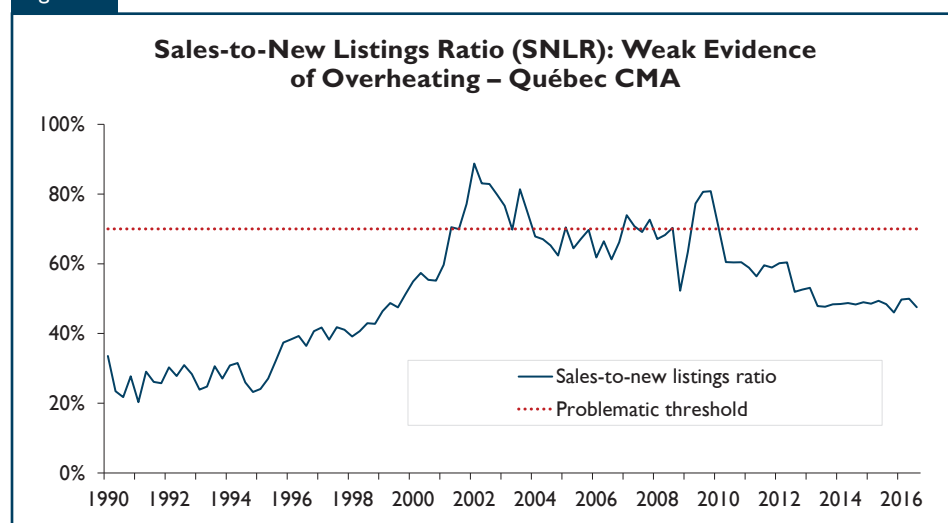
market was therefore sufficiently high so as not to raise any concerns with regard to overheating.

The relationship between supply and demand effectively indicated very soft market conditions in the condominium segment—a situation that has lasted since 2013. This was evidenced by another indicator of resale market conditions, that is, the active Centris® listings-to-sales ratio, which is available by market segment

(figure 2). As well, condominium supply significantly exceeded demand in all sectors of the CMA.

The relationships between supply and demand for the other housing types (single-family houses and plexes) also contributed to limiting the risks of overheating. In particular, easing

Figure 1



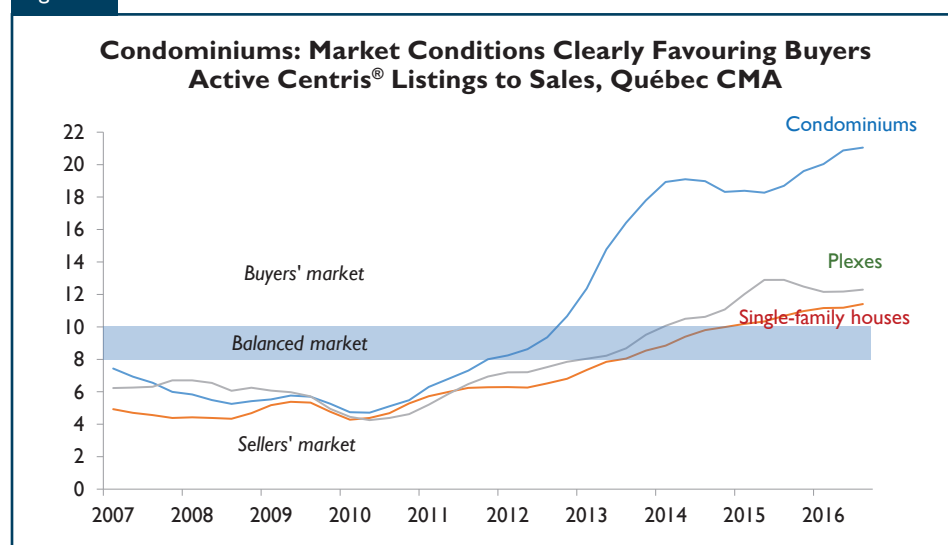
Sources: Quebec Federation of Real Estate Boards (QFREB) and CMHC calculations  
Last data point: Third quarter 2016

*“Our analytical framework revealed strong evidence of overvaluation in the Québec CMA. In fact, it appears that house prices are above the levels warranted by underlying demographic and economic fundamentals. As well, we are monitoring for the potential emergence of evidence of overbuilding, given that the number of conventional rental housing units under construction in the area remained high in 2016.”*



Elisabeth Koulouris  
Principal, Market Analysis

Figure 2



Source: QFREB by the Centris® system, four-quarter moving average  
Last data point: Third quarter 2016

market conditions were observed in the single-family home segment<sup>3</sup>, which accounts for 70 per cent of the transactions in the CMA. During the 12 months to the end of the third quarter of 2016, the numbers of single-family houses for sale rose slightly faster than the numbers of sales in most sectors of the metropolitan area. As a result, market conditions still favoured buyers in the third quarter of 2016.

## Price growth acceleration

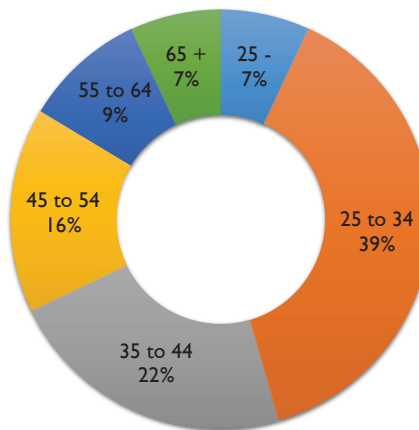
According to the HMA, evidence of price growth acceleration in the Québec CMA remained weak in the third quarter of 2016. In fact, the year-over-year growth<sup>4</sup> in the average Centris® price of residential properties was slightly negative for a third straight quarter. Overall, there was consequently no indication of price growth acceleration in the area.

The average price of residential properties has in fact stayed stable since 2014, as a result of the gradual easing of resale market conditions (see previous section), which has limited the growth in prices. This was particularly the case in the single-family home segment, for which the median selling price remained unchanged during the year preceding the third quarter of 2016.

For condominiums, there was even a decrease, of 3 per cent, in the median price during the year preceding the third quarter of 2016. This was not surprising, given the abundant supply on the resale market.

Figure 3

**First-Time Buyers (aged from 25 to 34) Account for a Significant Share of the Market**  
**Distribution of Buyers by Age Group – 2011, Québec CMA**



Source: Statistics Canada, Census, special compilation

## Overvaluation

The HMA results revealed strong evidence of overvaluation on the Québec CMA market in the third quarter of 2016, just like in the previous quarter.

It should be noted that the evidence of overvaluation does not reflect an acceleration in the growth of prices in recent quarters (see previous section) but rather indicates that prices are above the levels that could be expected given the economic and demographic fundamentals.

This is because the growth in prices was not fully supported by the changes in housing market fundamentals, including household income. For example, from 2002 to 2012, the average Centris® price in the Québec CMA more than doubled, while disposable income per capita rose by 55 per cent. The level

of prices gradually moved away from the level warranted by the economic and demographic trends in the area.

More recently, the decline in the population aged from 25 to 34, which began in 2015, contributed to curbing housing demand in the area. The people in this age group represented nearly two in five buyers on the Québec CMA market in 2011 (figure 3). The weaker demand among people aged from 25 to 34, combined with the other fundamentals, contributed to the emergence of strong evidence of overvaluation.

While there continued to be strong evidence of overvaluation in the third quarter, the signals have been tending to grow weaker since the beginning of 2016. The fact that the median price of condominiums decreased and the median price of single-family houses remained stable during the 12 months to the end of

<sup>3</sup> According to the Quebec Federation of Real Estate Boards (QFREB), during the 12 months to the end of the third quarter of 2016 (October 2015 to September 2016), active Centris® listings of single-family houses rose by 8 per cent, while sales edged up by 1 per cent. Supply therefore outpaced demand.

<sup>4</sup> Average price for the last 12 months.

the third quarter of 2016<sup>5</sup> helped gradually lessen the evidence of problematic conditions.

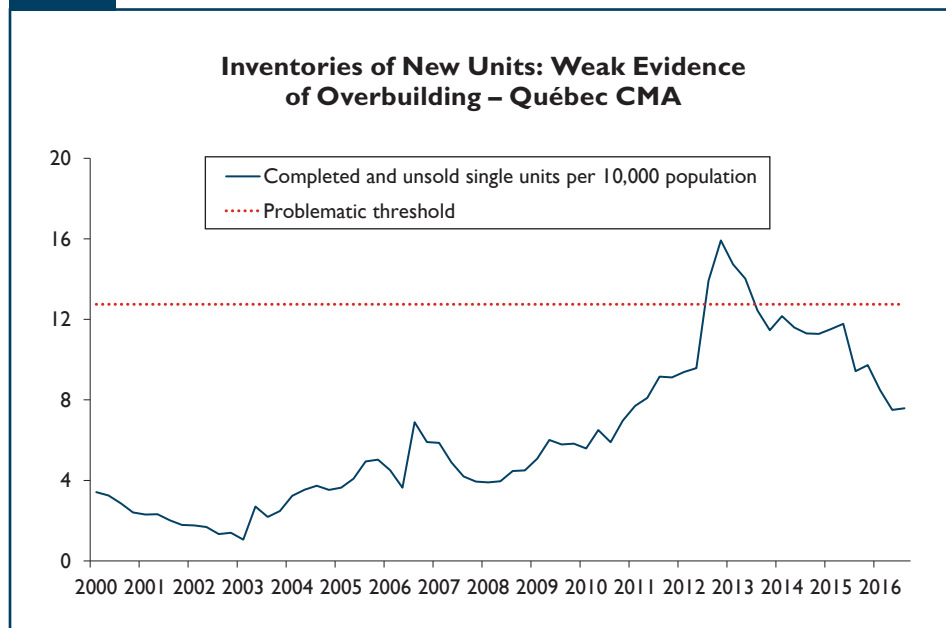
## Overbuilding

In the third quarter of 2016, the two indicators used to assess the risk of overbuilding, namely, the number of completed and unsold homeowner and condominium housing units per 10,000 population and the rental housing vacancy rate, were below their respective problematic thresholds. Overall, the HMA results therefore indicated weak evidence of overbuilding. However, while the first indicator is tending to move further and further away from the problematic threshold, the second is rather tending to move closer to that threshold.

On the one hand, after having peaked at the end of 2012, inventories of unsold new condominiums have been gradually absorbed, such that the number of completed and unsold units per 10,000 population in the CMA has followed a downward trend (figure 4). It was the slowdown in housing starts that allowed for the absorption of the recently completed units. The supply of condominiums still remains relatively significant, and low volumes of starts of this type are again expected over the coming years.

On the other hand, as shown by the results of the latest CMHC Rental Market Survey conducted in October 2016, the vacancy rate for conventional rental housing<sup>6</sup> is on the rise, having increased from 4.0 per cent in 2015 to 4.9 per cent in 2016 (figure 5). This hike was due

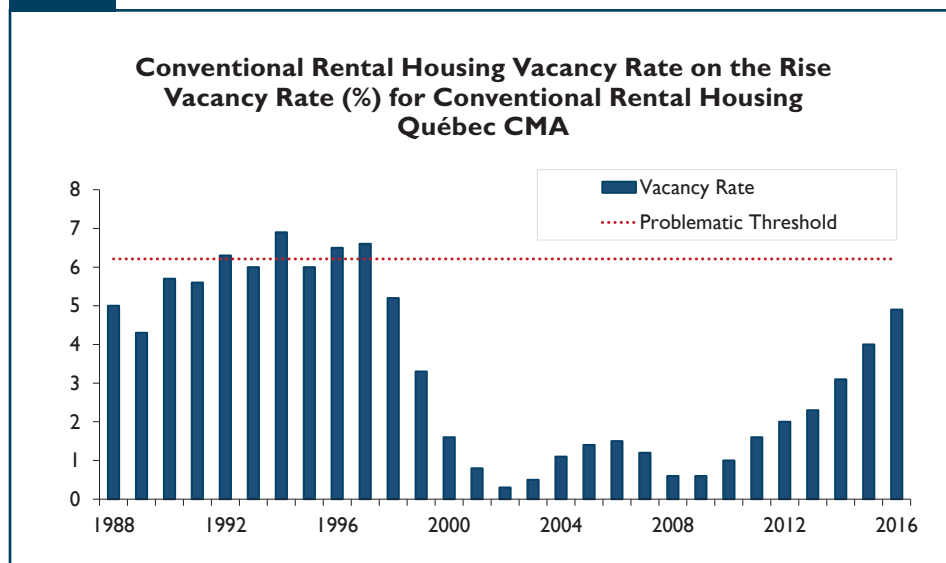
Figure 4



Source: CMHC

Last data point: Third quarter 2016

Figure 5



Source: CMHC

Last data point: 2016

<sup>5</sup> According to the QFREB, during the 12 months to the end of the third quarter of 2016 (October 2015 to September 2016), in the Québec CMA, the median price of condominiums decreased by 3 per cent from the same period a year earlier and the median price of single-family houses remained stable.

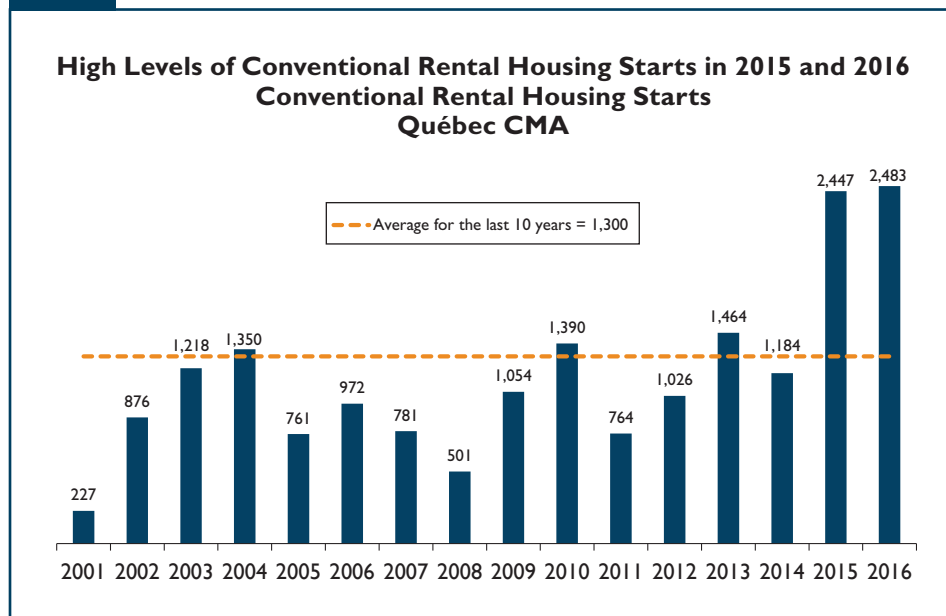
<sup>6</sup> Privately initiated apartments in rental buildings with three or more units, excluding seniors' housing units.

to the strong growth in the supply of conventional rental housing in the last two years. In fact, starts of this type hit an all-time high in 2015, and the pace of construction has remained just as strong in 2016.

More specifically, conventional rental housing starts reached 2,483 units in 2016 and 2,447 units in 2015, compared to an annual average of about 1,300 units for the last 10 years (figure 6). The relatively significant inventories of condominiums and the search for new markets in view of maintaining their levels of activity are among the factors motivating some developers who want to build rental housing projects, mostly sizable ones.

Consequently, although the vacancy rate is still below the problematic threshold, the clear upward trend in this rate should be monitored given the significant number of units that will be completed over the coming year.

Figure 6



Source: CMHC

Last data point: December 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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