

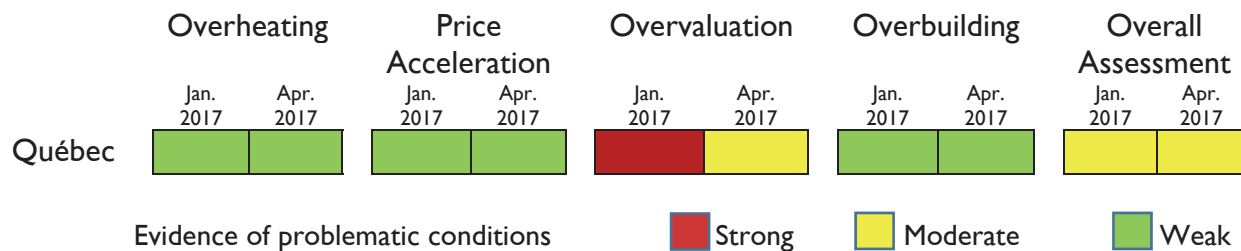
# HOUSING MARKET ASSESSMENT Québec CMA

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## Highlights



- Overall, the results from CMHC's Housing Market Assessment (HMA) still indicated moderate evidence of problematic conditions, with the situation having remained unchanged since the last issue was released in January 2017.<sup>1</sup>
- However, evidence of overvaluation shifted from strong to moderate, as a result of stronger fundamentals.
- The HMA did not detect any significant evidence of problematic conditions for the other factors assessed (overheating, price acceleration and overbuilding).
- But in a context where the vacancy rate is on the rise, the continued high level of rental housing construction should be monitored.
- The 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 summary of the framework can be found on page 7.

## 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 framework that considers the intensity of signals of imbalances (that is, how far the indicator is

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<sup>1</sup> Results are based on data as of the end of December 2016 and local market intelligence up to end of March 2017. 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 [Second Quarter 2016 National edition](#).

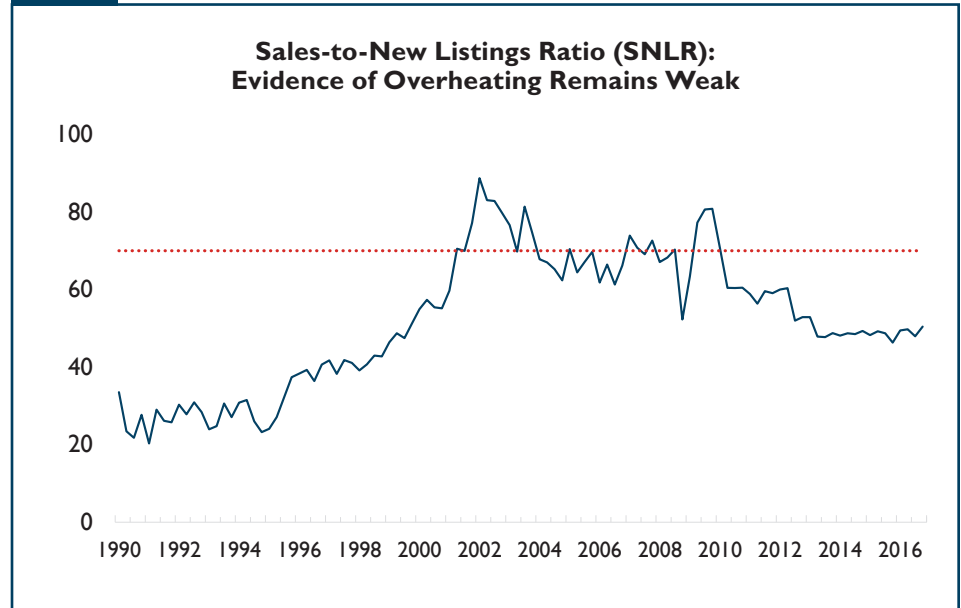
from its historical average) and the persistence over time. Generally, low intensity and persistence are associated with potential weaker evidence of problematic conditions. As the number of intense and persistent signals increases, the associated evidence of problematic conditions becomes stronger.

## In Detail

### Weak evidence of overheating

In the Québec census metropolitan area (CMA), the analytical framework detected weak evidence of overheating in the fourth quarter of 2016. Between the third and fourth quarters of 2016, the number of new listings on the resale market decreased slightly from the same period in 2015<sup>4</sup> (-1%), while sales showed a small increase (+2%)<sup>3</sup>. As a result, despite edging up, from 48%

Figure 1



Sources: Quebec Federation of Real Estate Boards (QFREB) by the Centris<sup>®</sup> system and CMHC calculations. Last data point: Fourth quarter 2016

to 50%, the sales-to-new listings ratio stayed well below the problematic threshold, estimated at 70%. Figure 1 shows that the situation remained stable over the past year.

While the results for overall Québec CMA housing market were below the problematic threshold for overheating, there were significant variations among the market segments. The numbers of active Centris<sup>®</sup> listings to sales effectively showed these differences. In the case of single-family homes, although supply increased, sales rose by 2% in the last quarter of 2016 over the same period in 2015, which contributed to stabilizing market conditions in that segment. In the condominium segment, there were 21 active Centris<sup>®</sup> listings per buyer on the market. Along with the continued significant supply in this segment, the decrease in sales

helped keep market conditions clearly favourable to condominium buyers, in all sectors of the CMA. Analysis of this indicator (active Centris<sup>®</sup> listings to sales) in these two market segments revealed no significant evidence of overheating, in either the overall market or the individual segments.

### Weak evidence of price acceleration

In the fourth quarter of 2016, evidence of price growth acceleration remained weak in the Québec CMA. The seasonally adjusted average Centris<sup>®</sup> price for all housing types stayed relatively stable between the third and fourth quarters of 2016.

Analysis of the price trends in 2016 revealed slightly different results depending on the housing types. For single-family houses, the median price

*“Overall, evidence of problematic conditions remained moderate. However, evidence of overvaluation shifted from strong to moderate, as a result of stronger fundamentals.”*



Tania Bourassa-Ochoa  
Senior Market Analyst

<sup>3</sup> According to the Quebec Federation of Real Estate Boards (QFREB), during the 12 months to the end of the fourth quarter of 2016.

<sup>4</sup> According to the Quebec Federation of Real Estate Boards (QFREB), during the 12 months to the end of the fourth quarter of 2016

<sup>5</sup> According to the Quebec Federation of Real Estate Boards (QFREB), during the 12 months to the end of the fourth quarter of 2016

showed a small gain (+1%). In the case of condominiums, as previously mentioned, the still relatively significant supply on the market led to a decline in the median price in 2016 (-4%), to \$190,000<sup>5</sup>. This was the third straight annual decrease in the median price of such dwellings on the resale market. Analysis by market segment did not show any evidence of problematic conditions for price acceleration, despite the differences noted.

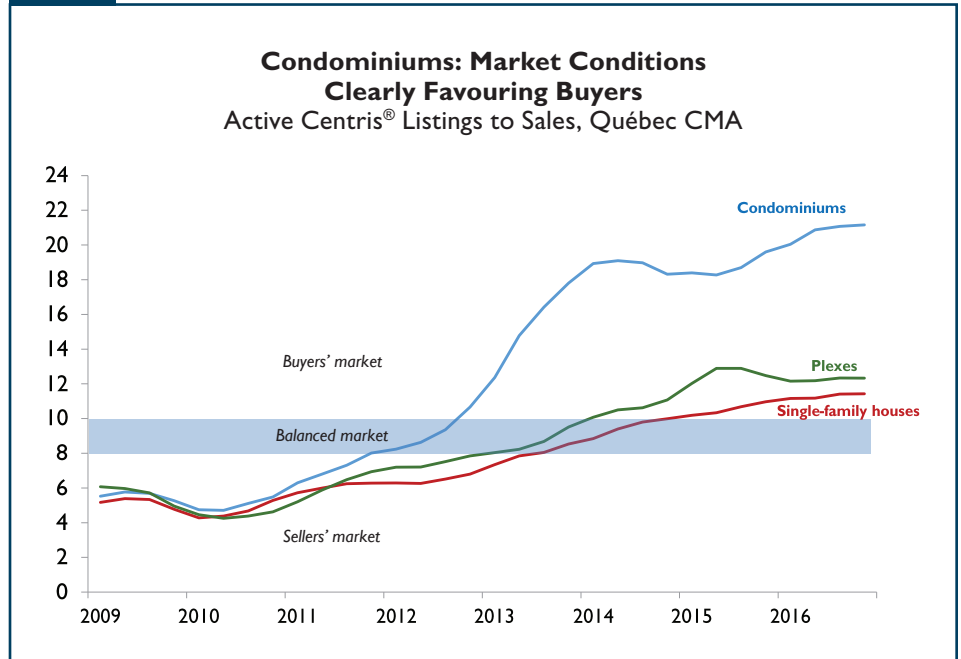
### Evidence of overvaluation shifts from strong to moderate

Evidence of overvaluation observed in the Québec area market shifted from strong to moderate in the last quarter of 2016. The assessment results indicated that fundamentals were better reflected in the house price levels.

Demographic factors continued to contribute to the evidence of overvaluation in the Québec CMA. Stagnant growth in the population aged 25 to 34, in particular, weakened housing demand gains.

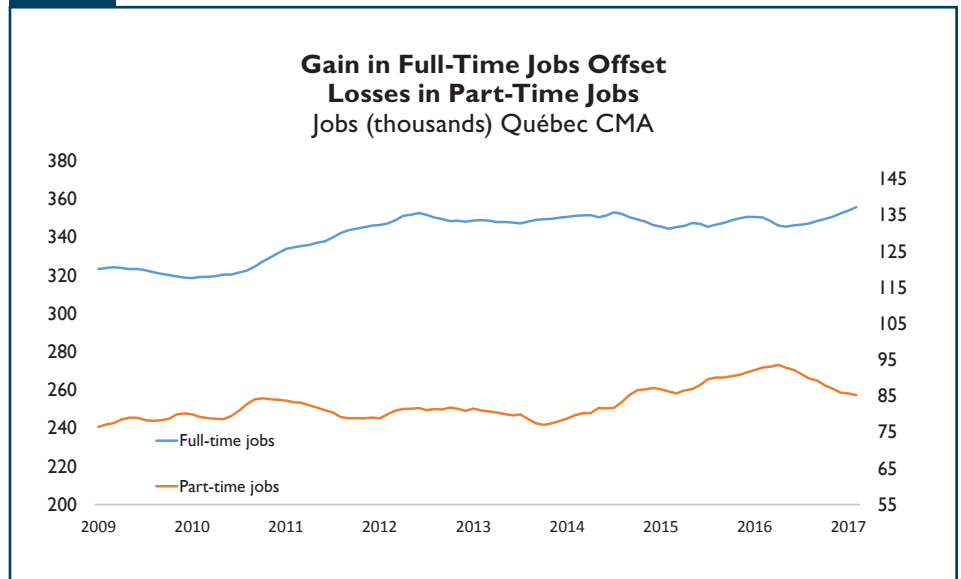
From an economic standpoint, however, the recent trends in employment and income explained the shift in the assessment results. In fact, even though the job numbers showed relative stability in 2016, employment among 25- to 44-year-olds posted a small gain (+1.3%), which was sufficient to move the indices<sup>6</sup>. Since this age group accounts for the bulk of first-time homebuyers, this gain—however slim—still helped lower the degree of overvaluation. Additionally, employment strengthened, as an upward trend in full-time jobs offset the losses in part-time jobs (see figure 3). With this improvement in employment,

Figure 2



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

Figure 3



Source: Statistics Canada, Labour Force Survey, 12-month moving average

personal disposable income per capita registered an increase, albeit small, of 1.5% over the past year, which also contributed to mitigating the signs of overvaluation in the Québec CMA.

The seasonally adjusted average Centris® price of residential properties was relatively stagnant in the fourth quarter of 2016, compared to the previous quarter. In fact,

<sup>6</sup> Labour Force Survey (LFS, Statistics Canada, Twelve month moving average, March 2017.

this was the second year in a row that the average price of residential properties remained rather stable. However, a review of recent changes in prices by housing type once again revealed some differences, as the median prices were down by 4% for condominiums and up by 1% for single-family houses. In the case of condominiums, the price drop was not insignificant, given the growing share of such dwellings in the overall housing market, and the situation was aggravated by the fact that the population aged 25 to 34 (representing 40% of condominium buyers) remained stable.

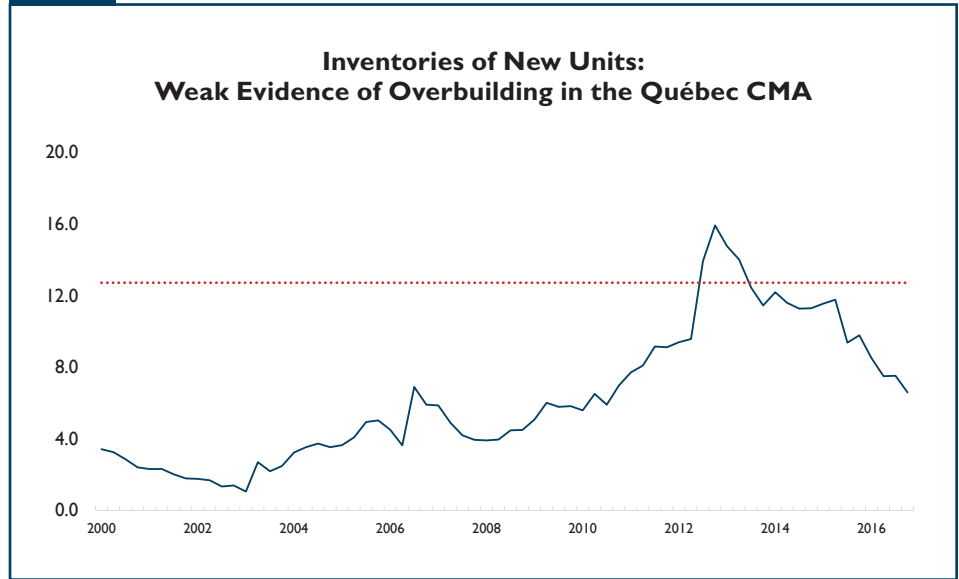
With the overall average price in the Québec CMA staying unchanged and employment regaining some ground, this resulted in moderate evidence of overvaluation in the fourth quarter of 2016.

### Weak evidence of overbuilding

In the last quarter of 2016, the HMA results still showed weak evidence of overbuilding in the Québec CMA. The assessment of this factor takes into account both the inventory of completed and unsold housing units in relation to the population and the proportion of vacant units on the rental market.

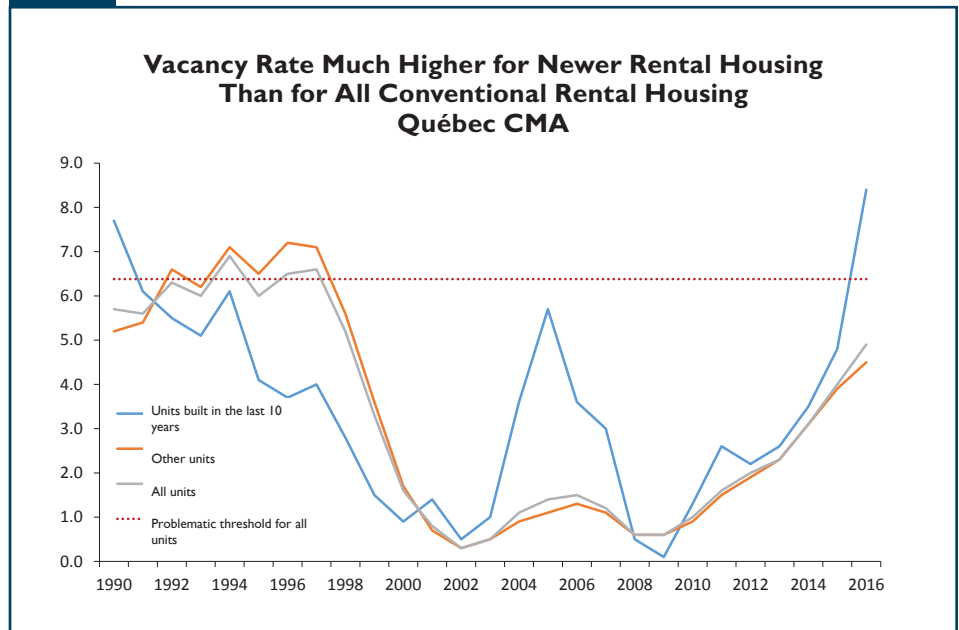
The inventory of new, completed and unabsorbed units (freehold and condominium) per 10,000 population continued to decrease, falling from 7.5 to 6.6. This result was attributable to a lower level of housing starts than in the past, especially in the case of condominiums. As was to be expected, the fact that condominium market conditions were clearly favouring buyers led to a decrease in the construction of such units, and starts of this type reached their lowest level in 15 years.

Figure 4



Sources: Statistics Canada and CMHC.  
Last data point: Fourth quarter 2016

Figure 5



Source: Statistics Canada, Labour Force Survey, 12-month moving average

In the case of rental housing, construction remained quite strong. The vacancy rate, while having remained below the problematic threshold, moved closer to that level with the increase recorded at the end

of 2016 (4.0% in 2015, versus 4.9% in 2016<sup>7</sup>). As well, a review of the vacancy rates by year of construction revealed that the proportion of vacant units was much higher for newly built units (in the last 10 years).

<sup>7</sup> Rental Market Survey, CMHC, October 2016.

In fact, the vacancy rate for these newer units rose from 4.8% in 2015 to 8.4% in 2016<sup>8</sup>. The significant level of rental apartment starts observed since 2015 strongly contributed to the increase in the vacancy rate. Figure 5 shows the recent increases in the overall vacancy rate and in the rate for units built in the last 10 years.

Given the relatively large number of rental housing units under construction, many apartments will be added to the current supply on the conventional rental market and increase competition in that market. As a result, a subsequent easing of the rental market, especially in the case of newer buildings, cannot

be ruled out. Considering the high level of conventional rental housing construction in the area and the clear upward trend in the vacancy rate, the situation should be monitored closely.

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<sup>8</sup> Rental Market Survey, CMHC, October 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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The screenshot shows a grid of news items with dates and headlines. Visible headlines include: 'The HMI Portal provides reliable and impartial housing market reports, data and analysis.', 'An alternative water ready home — what's the plan?', 'We have to learn to be flexible... and so does our housing', and 'What is a condo? a) An apartment b) A single family home c) A townhome d) All of the above.' At the bottom, there is a red banner with the subscription information and a social media sharing icon.