

HOUSING MARKET ASSESSMENT

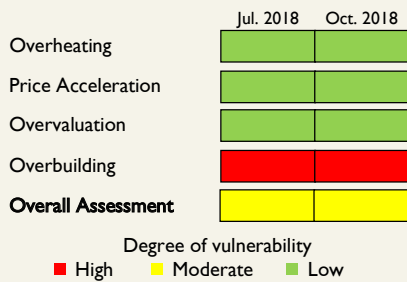
Edmonton CMA

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Highlights

Results Overview Edmonton CMA



- CMHC's HMA Framework continued to detect a moderate degree of vulnerability in the overall assessment for Edmonton¹.
- Evidence of overvaluation remained low as Edmonton experienced stronger economic and demographic fundamentals and lower house prices.
- The inventory of completed and unsold units and the rental vacancy rate both remained above their respective thresholds indicating overbuilding. Unsold inventories were persistent among single-detached units.
- There was low evidence of overheating and price acceleration.

HMA Overview²

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 degrees of vulnerability 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 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 degree of market vulnerability. The HMA is a comprehensive framework that considers both 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 low evidence of vulnerability. As the number of intense and persistent signals increases, the associated degree of vulnerability becomes stronger.

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¹ Results are based on data as of the end of June 2018 and local market intelligence up to the end of September 2018. CMHC continuously monitors market developments and will issue HMA updates on a quarterly basis.

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

In Detail

Overheating

The Housing Market Assessment (HMA) framework detected low evidence of overheating in the Edmonton housing market as the sales-to-new listings ratio (SNLR) declined in the second quarter of 2018 to 40% from 48% in the previous quarter, which was well below the 85% critical threshold, and indicative of buyers' market conditions. The SNLR dropped as a result of a 7% quarter-over-quarter (q/q) decline in seasonally adjusted sales combined with an 11% q/q increase in seasonally adjusted new listings. The SNLR has ranged between 40% and 55% since the beginning of 2015.

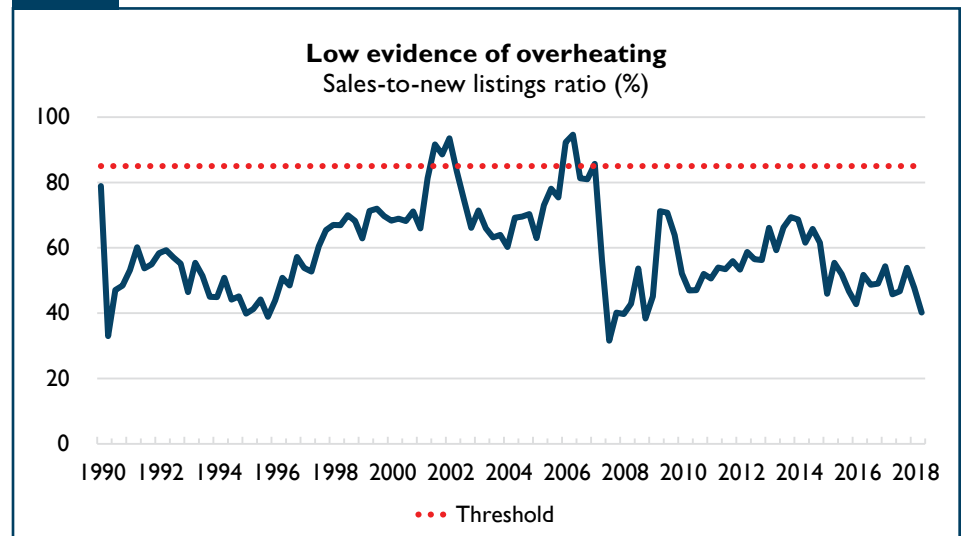
Price Acceleration

CMHC's indicator for price acceleration continued to detect low evidence of price acceleration in the second quarter of 2018. The real MLS® average price and

the real Teranet® house price index both decreased on a year-over-year basis. The MLS® average price, in particular, has experienced modest year-over-year declines for most

of 2018. This can largely be attributed to the condominium segment where average condominium prices have declined more than other segments of the market³.

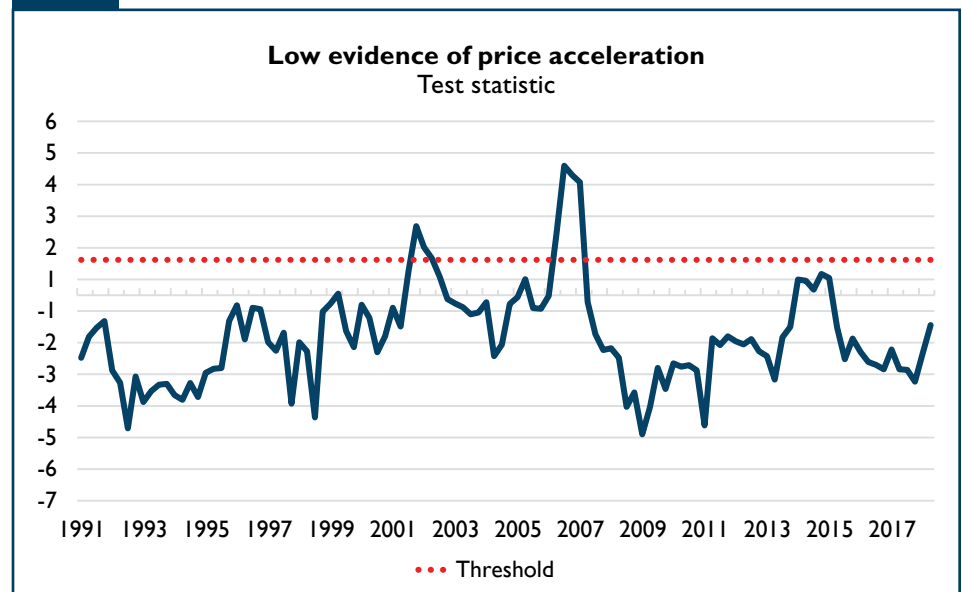
Figure 1



Last data point: 2018Q2

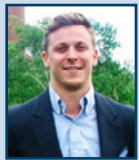
Sources: CREA and calculations (threshold) by CMHC

Figure 2



Last data point: 2018Q2

Sources: CREA and calculations by CMHC



James Cuddy,
Senior Analyst,
Economics

The Housing Market Assessment continued to indicate a moderate degree of overall vulnerability in Edmonton due to overbuilding being detected. Inventories of single-detached units continued to rise, while on the other hand, unabsorbed inventory for row and apartment units dipped.

³ Edmonton Real Estate Board (EREB).

Overvaluation

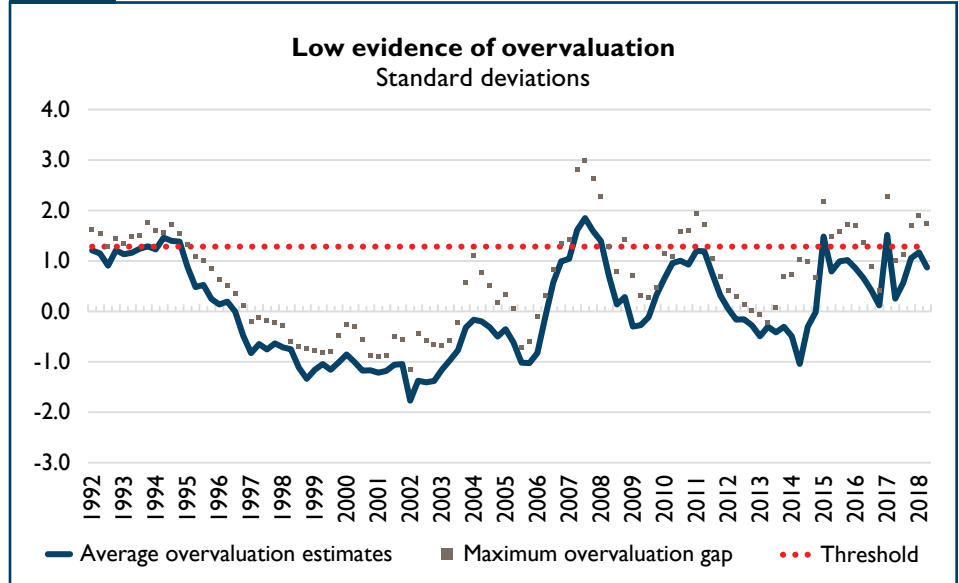
CMHC's HMA framework detected low evidence of overvaluation in Edmonton in the second quarter of 2018. The average gap between actual house prices and price levels estimated by economic and demographic fundamentals were below the critical threshold that would indicate overvaluation.

Buyers' market conditions have lowered house prices in Edmonton. At the same time, Edmonton has experienced growth in economic and demographic fundamentals. The adult population aged 25 to 34, a proxy for household formation and first-time buyers, grew in the second quarter of 2018 from the first quarter. In addition, year-over-year real personal disposable income increased, reflecting the continued recovery of Edmonton's labour market. As a result of stronger fundamentals, combined with lower housing prices, all but one of CMHC's overvaluation models declined from last quarter, indicating that housing values in Edmonton have moved closer in line with economic and demographic fundamentals in Edmonton.

Overbuilding

There continued to be strong evidence of overbuilding in Edmonton as elevated inventory levels per capita persisted in the second quarter of 2018. This market imbalance is being largely driven by construction activity among single-detached units coupled with rising choices for buyers in the resale market. Recent monthly data indicates that elevated inventory levels among the single-detached segment are likely to persist into the third quarter of 2018. On the other hand, unabsorbed inventory

Figure 3

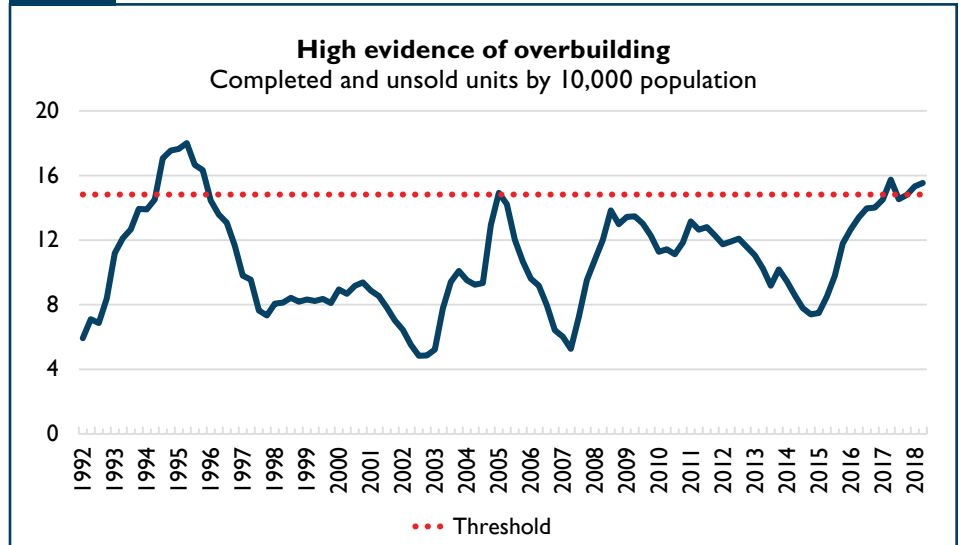


Last data point: 2018Q2

Sources: CREA, Statistics Canada and calculations by CMHC.

Note: The average estimate of overvaluation is the average gap between actual house prices and price levels estimated from a group of selected models. Baseline models include demand, supply, hybrid, and affordability models, each of which is estimated using four measures of house prices to generate sixteen unique estimates of overvaluation. The selection of models is conducted with a set of cointegration tests, and the selected models are estimated with Dynamic Ordinary Least Squares (DOLS). The maximum overvaluation gap is obtained from the model that has the largest gap between the actual price and the estimated price. The threshold is fixed at a critical value of 1.29 for a confidence level of 80%. Overvaluation is signaled when overvaluation estimates lie above the threshold.

Figure 4

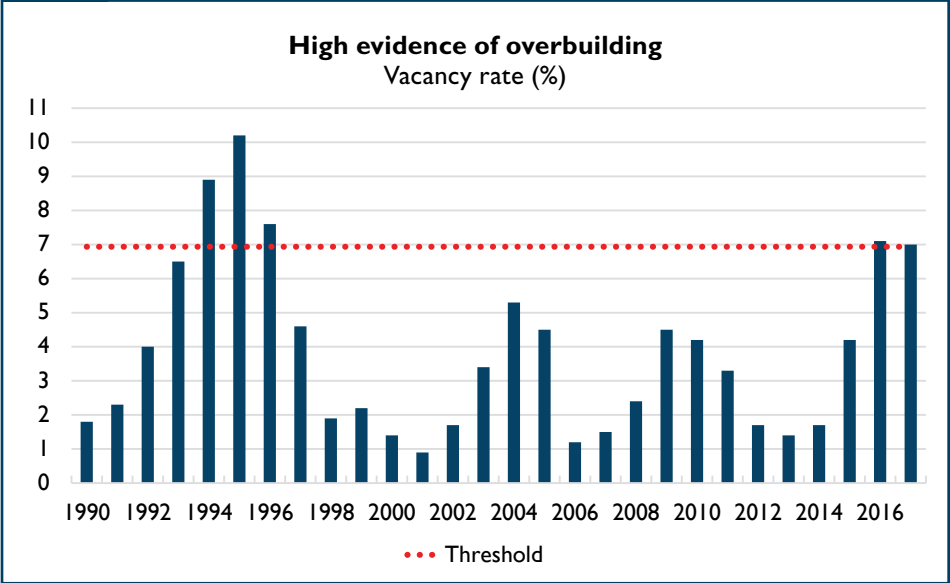


Last data point: 2018Q2

Sources: Statistics Canada and CMHC

for row and apartment units has dipped below the problematic threshold indicating that the multiples segment of the market is moving toward a more balanced state. Driving this trend has been a declining number of row and apartment starts combined with support from recently stronger employment growth among young adults.

Figure 5



Last data point: 2017
Sources: CMHC

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 detect imbalances in housing markets.

Specifically, the framework considers four main factors that may provide an early indication of vulnerability in the housing market: (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 incidence of signs of vulnerability, 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 a low degree of vulnerability. Conversely, as the intensity, number, and/or persistence of the signals increases, so does the evidence of imbalances in the housing market.

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 vulnerability. 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 vulnerable 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 vulnerabilities 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 signs of overheating, 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 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 signs of overbuilding 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 degree of market vulnerability. The HMA reflects a comprehensive framework that not only tests for the presence or incidence of signals of imbalances (that is, how far the indicator is from its historical average), but also considers the intensity and the persistence of these signals over time. Generally, low intensity and persistence are associated with a lower vulnerability. As the number of persistent signals increases, the evidence of an imbalance 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 that can identify imbalances. 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 showing vulnerability 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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