

# HOUSING MARKET ASSESSMENT

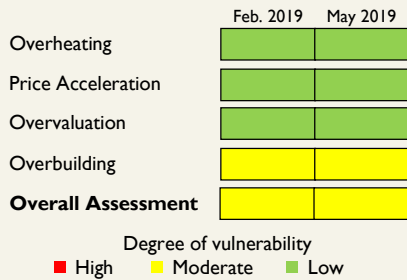
Saskatoon CMA

Date Released: Second Quarter 2019



## Highlights

### Results Overview Saskatoon CMA



- The Saskatoon housing market continues to exhibit a moderate degree of vulnerability.<sup>1</sup>
- Low evidence of overvaluation in house prices is maintained.
- The ratings on overheating and house price acceleration are unchanged.
- Moderate evidence of overbuilding is still signaled despite the pullback in housing starts.

## 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 and contribute to an orderly adjustment of housing market imbalances.

The HMA is an analytical framework that provides a comprehensive view of housing market vulnerabilities. It should be noted that it intends to identify imbalances in the housing market; it is not aimed at being a framework to identify long-term fundamental affordability challenges.

It considers four main factors: overheating, price acceleration, overvaluation and overbuilding. Overheating is detected when sales greatly outpace new listings in the market for existing homes. Price acceleration is signaled when the growth rate of house prices increases rapidly. Overvaluation indicates that house prices are elevated compared to price levels supported by personal disposable income, population, interest rates, and other fundamentals<sup>3</sup>. Overbuilding is flagged when the rental apartment vacancy rate and/or inventory of newly built and unsold housing units are significantly above normal levels.

The HMA combines the results from a technical framework with insights gained through CMHC's market

analysts' knowledge of local market conditions. These insights allow CMHC to provide additional context and interpretation to the results of the HMA framework.

Colour codes indicate the degree of market vulnerability. The HMA is a comprehensive framework that considers both the intensity (magnitude) and the persistence of signals of imbalances. 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 higher.

<sup>1</sup> Results are based on data as of the end of December 2018 (the annual rental apartment vacancy rates are from October 2018) and local market intelligence up to the end of March 2019.

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

<sup>3</sup> Other fundamental factors include mortgage-borrowing capacity of households, required minimum down payment, and labor productivity.

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## In Detail

### Low evidence of overheating is unchanged

We have maintained the rating on overheating. The pace of existing home sales slowed more than that for new listings in the final quarter of 2018, nudging the seasonally adjusted sales-to-new-listings ratio (SNLR) lower to 39% from 41% in Q3 2018. At this level, the SNLR remained significantly below the framework's threshold for overheating of 85%. Collectively, stricter mortgage qualifying rules, rising interest rates and a mixed economic performance have moderated demand for resale homes in Saskatoon. Along with persistent downward pressure on residential prices, this has resulted in some potential home sellers staying on the sidelines for the time being.

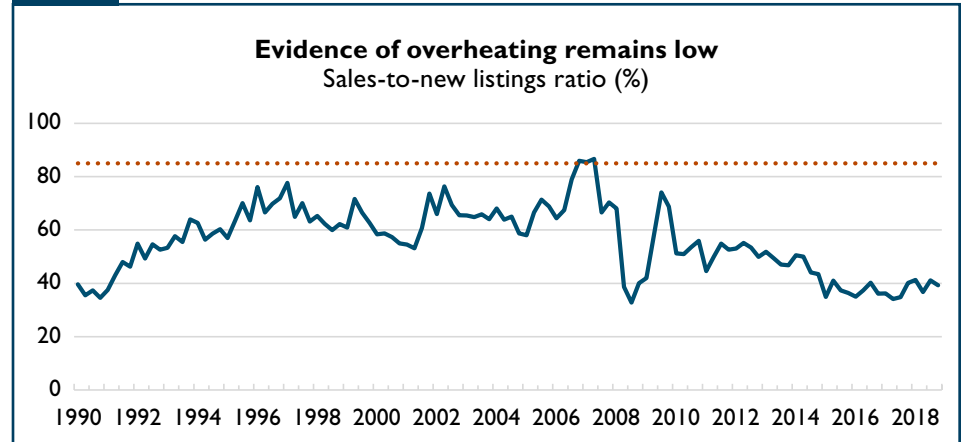
### Evidence of price acceleration is maintained

A low rating on price acceleration remains for the broader Saskatoon market. The decline in house prices slowed down somewhat during

the final quarter of 2018, with the inflation-adjusted MLS® average price relatively stable compared to the same period in 2017. However,

Saskatoon's MLS® HPI composite benchmark price<sup>4</sup> declined to \$293,200 in Q4 2018 from \$294,300 in Q3 2018, and was down 0.8% from a year earlier.

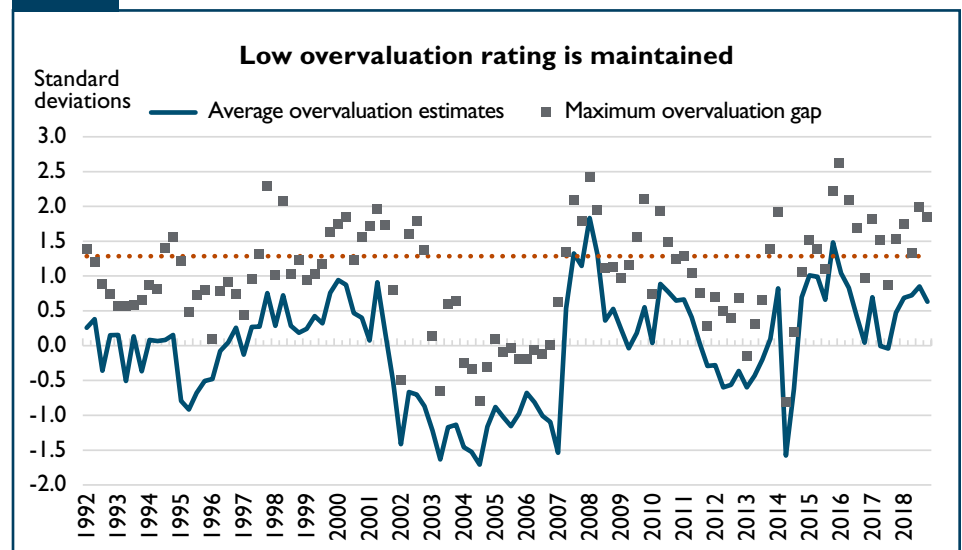
Figure 1



Last data point: 2018Q4

Sources: CREA (seasonally adjusted) and calculations (threshold) by CMHC

Figure 2



Last data point: 2018Q4

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.



Goodson Mwale  
Senior Analyst  
Economics

*"The HMA framework continues to detect a moderate degree of vulnerability in Saskatoon's housing market. While the ratings on overheating, accelerating prices and overvaluation remain low, an elevated annual rental vacancy rate above its critical threshold signals moderate overbuilding."*

<sup>4</sup> Source: CREA. The MLS® HPI is based on a hybrid model that merges repeat-sales and hedonic price approaches, and reflects the contribution made by various quantitative and qualitative housing features toward the home price.

In the single-detached segment, the MLS® HPI benchmark price edged lower in Q4 2018 from Q3 2018, but was up marginally on a year-over-year basis. The benchmark prices for row and apartment units were both down by more than 5.0% in the fourth quarter of 2018, compared to the same period in 2017.

## Overvaluation rating is maintained

Despite an improving post-recession labour market, the performance of underlying fundamentals have remained mixed over the past several quarters. Saskatoon's young adult population increased by 1.8% in Q4 2018 from Q4 2017. However, this gain was offset by a 1.7% decrease in the inflation-adjusted personal disposable income over the same period. As such, the gap between observed house prices and those estimated for economic and demographic factors remains relatively narrow, signaling low evidence of overvaluation. In addition, figure 2 shows that the average estimate of overvaluation obtained from a group of selected models decreased in Q4 2018, and remained below the framework's critical threshold for this factor.

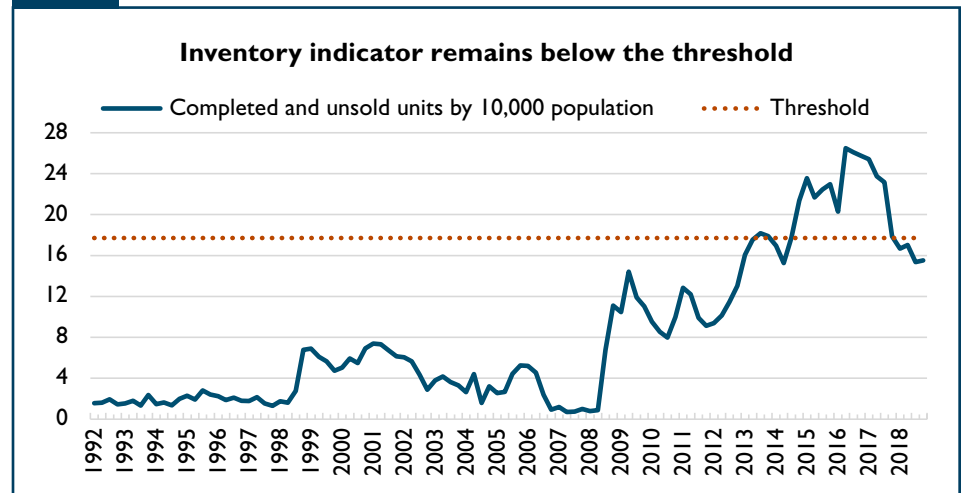
## Moderate overbuilding rating is unchanged

We have maintained our assessment of moderate evidence of overbuilding in Saskatoon's market. The inventory of completed and unsold housing units in the ownership and condominium markets has been on a declining trend since early 2016. This is particularly the case in the multi-unit segment where inventory levels had risen

significantly during the construction boom period. Given the slowdown in housing starts over the past two years, local homebuilders have been actively directing demand towards unsold inventory before starting new projects. In Q4 2018, the inventory of new housing units remained below the framework's critical threshold.

On the other hand, Saskatoon's annual rental vacancy rate of 8.3% in 2018 was above its critical threshold of 7.69%. As this indicator is complimentary to the framework's overall assessment for overbuilding, the moderate rating was maintained in the current release.

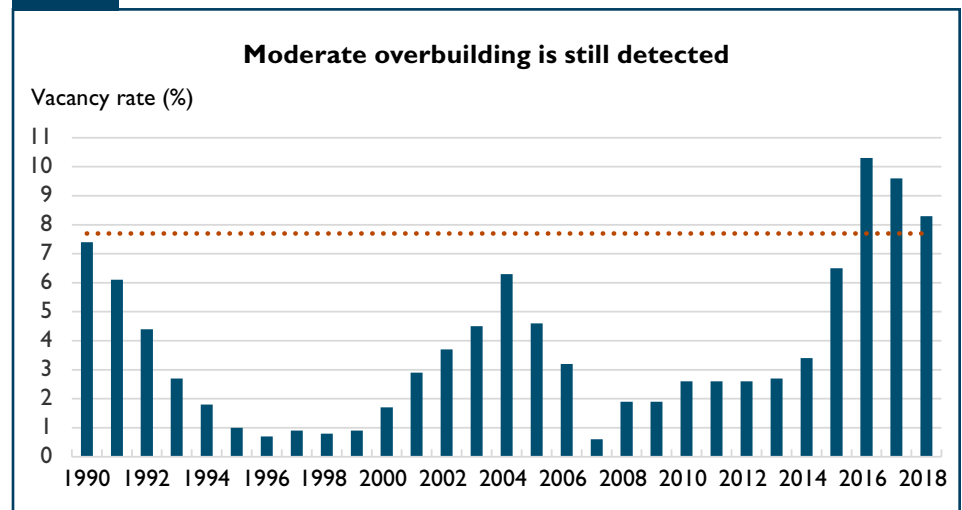
Figure 3



Last data point: 2018Q4

Sources: Statistics Canada and CMHC

Figure 4



Last data point: 2018Q4

Sources: CMHC, calculations (threshold) by 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. 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 in the existing home market; (2) sustained acceleration in house prices meaning that the rate of increase in prices is itself increasing; (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 the intensity (magnitude) and the persistence of signals. 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 number, intensity, 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 recent 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 in the resale market. The sales-to-new listings ratio is used as an indicator to assess possible overheating conditions. 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.

### Acceleration in House Prices

House price acceleration occurs when the growth rate in house prices continuously increases. Acceleration in house prices over an extended period would

lead prices to unsustainable levels, hence increasing housing market vulnerability. To assess acceleration in house prices, the HMA framework uses a statistical test\* that was developed to identify periods of accelerating growth in 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—based on economic theory—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 apartment vacancy rate, and the inventory of completed and unsold housing units per 10,000 population. The HMA framework compares the current levels and recent trends in these indicators with thresholds.

**Note 1:** Colour codes indicate the degree of market vulnerability. Overheating and price acceleration are each assessed with a single indicator. Colour scales for these factors vary between green and yellow only. Overvaluation and overbuilding are assessed with multiple indicators. Their colour scales, as well as the colour scale for the overall assessment, change among green, yellow and red to reflect different degrees of imbalances.

**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:** 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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