

HOUSING MARKET ASSESSMENT

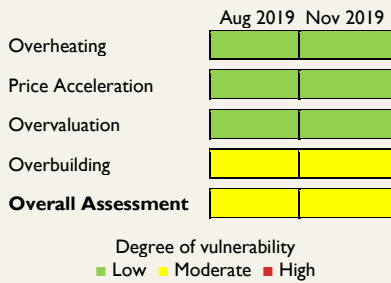
Edmonton CMA

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Highlights

Main HMA Results Edmonton



- CMHC’s Housing Market Assessment (HMA) framework detected a moderate degree of vulnerability in the overall assessment for Edmonton.¹
- Evidence of overbuilding remained moderate. While the rental market has begun tightening in Edmonton, absorption has yet to catch up with production level, pushing unsold home inventory to a record high level.
- Elevated and rising inventory in the ownership market combined with declining home price and weakened employment market, contributed to 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 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 fundamentals³. 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.

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¹ Results are based on data as of the end of June 2019 (the annual rental apartment vacancy rates are from October 2018) and local market intelligence up to the end of September 2019.

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

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

In Detail

Low Evidence of Overheating

CMHC’s HMA framework continued to detect low evidence of overheating in Edmonton in the second quarter of 2019 as the sales-to-new-listing ratio (SNLR) remained well below the critical threshold of 85%. On a year-over-year basis, sales increased by 3% while new listings decreased by 12%. Compared to Q1 2019, both sales and new listings trended up, following a similar seasonal pattern often observed in the second quarter of the past few years. However, sales activities grew at a faster pace than the growth of new listing did, which contributed to slightly higher SNLR compared to last quarter. Active listings have also gone down by 11% compared to Q2 2018. While single detached remains the majority of the listed homes, apartment listings were absorbed at a faster pace than other home types, indicating a shift in preference towards a more affordable segment of the resale market.

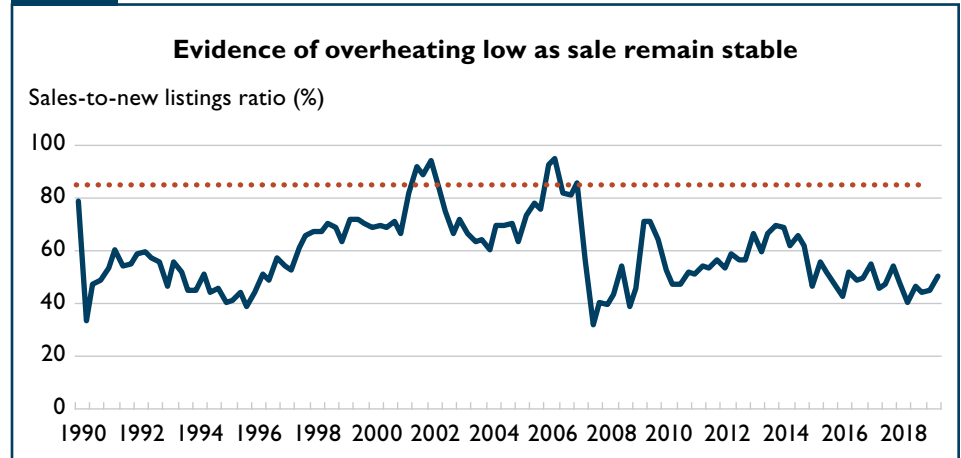
Although sales activities trended up slightly compared to the same quarter last year, the resale market continued to face uncertainties as



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“Edmonton’s housing market remains moderately vulnerable. Continued pressure around homeowner affordability due to economic challenges across the province has led homebuyers to focus on lower-priced segment of the market, pushing inventories higher as production level continues to outpace absorptions.”

Figure 1



Sources: CREA and calculations (threshold) by CMHC

the economy remained in recovery mode since the past recession. As of Q2 2019, the unemployment rate was 6.9%, the highest since Q4 2017. Correspondingly, the inflation adjusted personal disposable income declined slightly on a year-over-year basis. The slow recovery of the job market, combined with a relatively low and stable SNLR, have kept Edmonton in buyers’ market conditions.

Low Evidence of Price Acceleration

The low rating of price acceleration remained in the second quarter of 2019 for Edmonton. The elevated inventory, combined with softened demand and slow job growth, contributed to continued downward trends in prices, as reflected by various price indexes adopted in the HMA framework. The inflation adjusted average MLS® price declined year-over-year, along with the Teranet® House Price Index and the New Housing Price Index, indicating a general cooling condition in both new home and resale home segments of the ownership market.

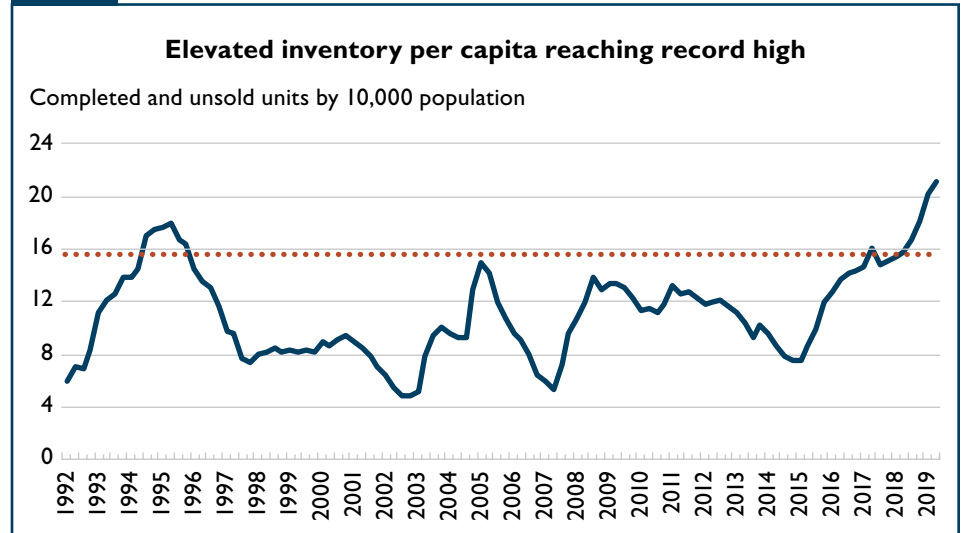
Low Evidence of Overvaluation

The HMA framework continued to detect low evidence of overvaluation in the second quarter of 2019. Both of the max and the average gap between actual home price and estimated home price were below zero in Q2 2019. The models adopted in the framework take into consideration a number of factors including population growth, personal disposable income, mortgage rate, carrying cost for homeowners, and labour productivity (construction sector). As a proxy of household formation, the young adult population aged 25 to 34, was one of the factors adopted in most of the models. As a result, a modest year-over-year increase of the young adult population in Edmonton led to a higher model-estimated price relative to actual market price. The model that estimated lower home price relative to actual home price utilized down payment as one of the factors in the estimation process. This is in line with the softened job market and income growth seen in Edmonton in Q2 2019, reflected through declining disposable personal income and upward trending unemployment rate.

Moderate Evidence of Overbuilding

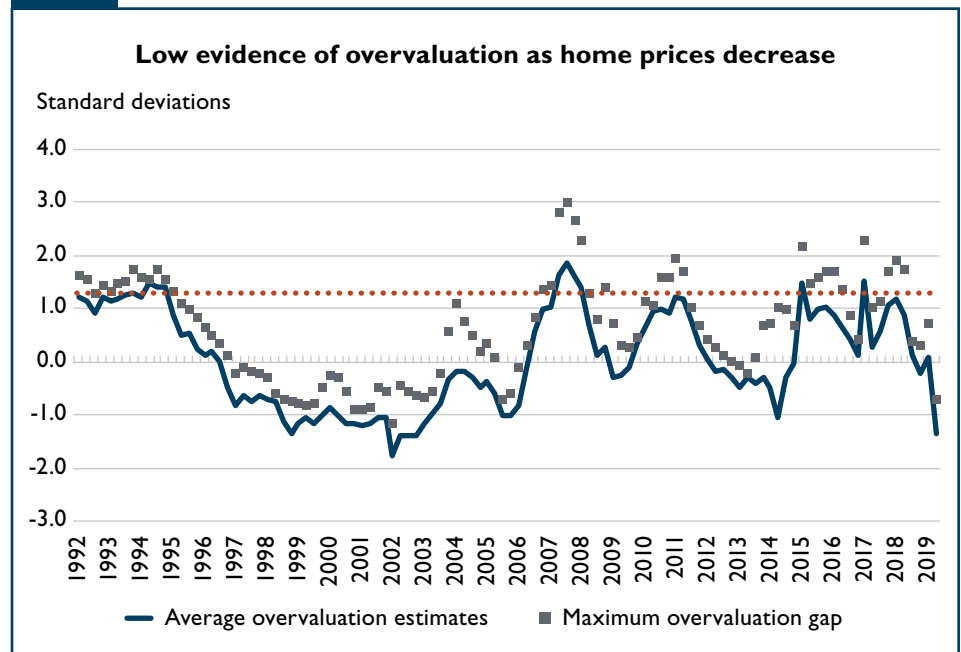
Edmonton continued to indicate moderate evidence of overbuilding. While the rental market began tightening in Edmonton by year-end 2018, the imbalance between supply and demand in the ownership market has grown stronger. Inventory of completed and unsold units (per 10,000 population) continued to grow on an upward trend that started in Q3 2017, reaching 21, a level not seen since 1992. The majority of the unabsorbed inventory are single-detached homes, indicating a relatively weakened demand in the higher priced segment of the market. In the rental market, a few new purpose-built rental projects went underway in Q2 2019, representing an 13% increase of rental starts compared to last quarter. This could ease rental market in the next few quarters, as these projects become available to renters. Albeit elevated inventory on the resale market, since vacancy rate fell below the critical threshold in 2018, Edmonton maintains a moderate rating of overbuilding in Q2 2019.

Figure 2



Sources: Statistics Canada and CMHC

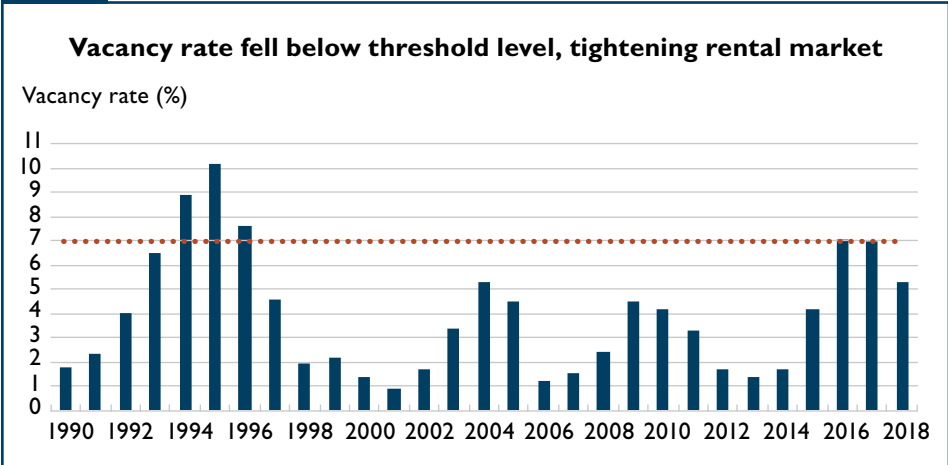
Figure 3



Sources: CREA, Statistics Canada, Teranet and National Bank of 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. These include demand, supply, hybrid, and affordability models (as of the fourth quarter of 2019, there are five models in total), each of which is estimated using four measures of house prices to generate twenty unique estimates of overvaluation. The selection of models is conducted with a set of cointegration tests, and the selected models are estimated with Dynamic Seemingly Unrelated Regression (DSUR). 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 1.285 for a confidence level of 80%. Overvaluation is signaled when overvaluation estimates lie above the threshold.

Figure 4



Source: 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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