UBS Swiss Real Estate Bubble Index 2Q 2021

UBS Swiss real estate bubble index

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- The *UBS Swiss Real Estate Bubble Index* measures the risk of a real estate bubble in the Swiss residential housing market.
- The index rose to 1.90 points in the second quarter of 2021, driven by a rapid rise in prices in the Swiss residential housing market.
- Growth in household mortgage debt has also gradually increased in recent months. However, the index is forecast to fall back slightly by the end of the year.

Quellen: Mauro Mellone, UBS

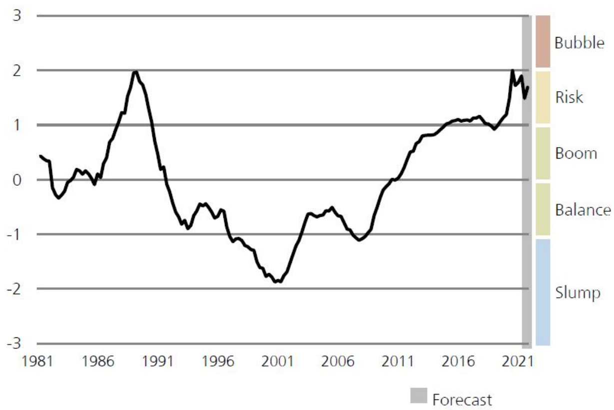
The *UBS Swiss Real Estate Bubble Index* rose slightly from 1.78 to 1.90 points in the second quarter of 2021, remaining in the risk zone. The increase was driven by large price increases in the residential housing market and accelerated growth in household mortgage volumes.

Households going deeper into debt

Residential housing prices rose 5.4 percent year-on-year in the second quarter of 2021. This is the largest increase in eight years. Income growth was unable to match that pace. Pre-COVID-19, the average price of a residential property was just under 6.5 times annual income. Today, it probably runs around 7.1 times annual income. Home affordability has thus deteriorated further.

Growth in outstanding mortgages to private households has accelerated constantly in recent months. Mortgage volumes are nearly 3 percent higher today than they were a year ago. The growth rates are still well below their historical all-time highs, but any further acceleration would be a warning signal: A combination of debt increased boom and rapid price growth has almost always been a harbinger of growing imbalances, whether in Switzerland or worldwide.

UBS Swiss Real Estate Bubble Index



Quelle: UBS

Index calculation: The UBS Swiss Real Estate Bubble Index comprises six sub-indices. It is calculated as the weighted average of standardized indicators, using primary component analysis, and shows the deviation in standard deviations from the average, which is standardized to zero.The index uses the following classification: Slump (below -1), Balance (from -1 to less than 0), Boom (from 0 to less than1), Risk (from 1 to less than 2) and Bubble (2 and upwards).

Investment demand remains strong

At the same time, offering rents have fallen 3.2 percent year-on-year—the steepest drop since 1996. The widening gap between residential property prices and apartment rents has exacerbated risks, particularly in the buy-to-let segment. Achievable returns have fallen to record lows, but investment demand remains buoyant. The expectation of further price increases is the main motivation for investing in buy-to-let properties.

The economic recovery in the second half of the current year should prevent the index from rising into the bubble risk zone for now, in our view. We currently expect an index level of 1.69 for the final quarter of 2021, which is below the current level. This year-end forecast value was introduced due to the volatility in current data (see comment below). However, once the pandemic fades, we expect the residential housing market imbalances to be considerably higher than before the crisis.

Comment: Business restrictions due to COVID-19 continue to cause considerable volatility in the economic performance. This has led to major fluctuations in our model-based assessment of the real estate bubble risk for the Swiss residential housing market. Due to this volatility, we will, for the time being, present the expected trend in the UBS Swiss Real Estate Bubble Index until the end of the year based on our forecasts for the performance of the economy and the real estate market.

UBS Swiss Real Estate Bubble Index

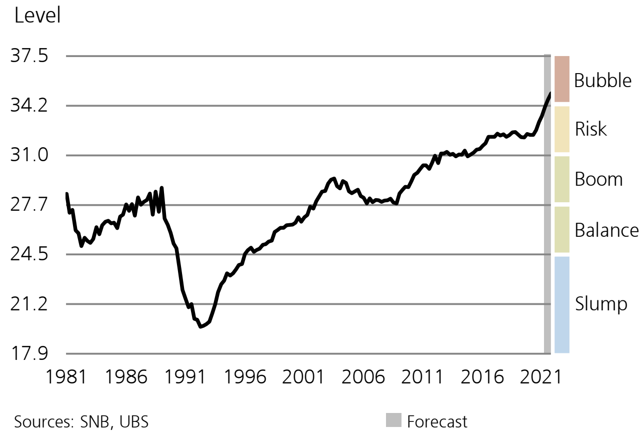
Year	Period	Index	Trend
2016	Quarter 1	1.10	Decrease
	Quarter 2	1.07	Decrease
	Quarter 3	1.08	Increase
	Quarter 4	1.09	Increase
2017	Quarter 1	1.07	Decrease
	Quarter 2	1.13	Increase
	Quarter 3	1.13	Unchanged
	Quarter 4	1.16	Increase
2018	Quarter 1	1.10	Decrease
	Quarter 2	1.03	Decrease
	Quarter 3	1.02	Decrease
	Quarter 4	0.98	Decrease
2019	Quarter 1	0.92	Decrease
	Quarter 2	0.98	Increase
	Quarter 3	1.07	Increase
	Quarter 4	1.13	Increase
2020	Quarter 1	1.19	Increase
	Quarter 2	1.48	Increase
	Quarter 3	2.00	Increase
	Quarter 4	1.73	Decrease
2021	Quarter 1	1.78	Increase
	Quarter 2	1.90	Increase
	Quarter 3	1.48	Decrease (forecast)
	Quarter 4	1.69	Increase (forecast)

- Increase compared to the previous quarter
- Decrease compared to the previous quarter
- Unchanged
- Forecast

Sub-indexes of the UBS Swiss Real Estate Bubble Index

Home prices to annual rents

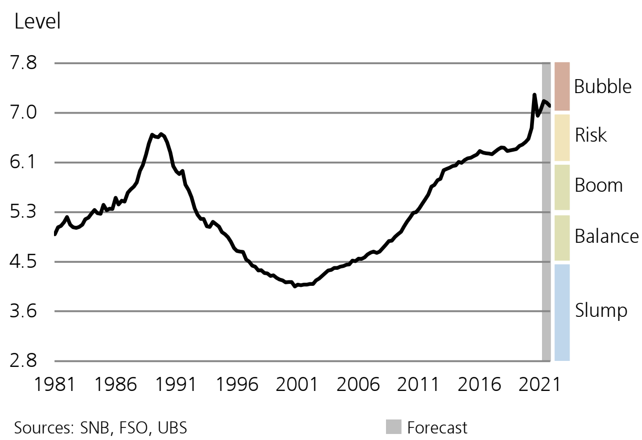
An above-average price-to-rent ratio indicates a high dependency on sustained low interest rates or implies expectations of price increases.



Sources: SNB, UBS

Home prices to household income

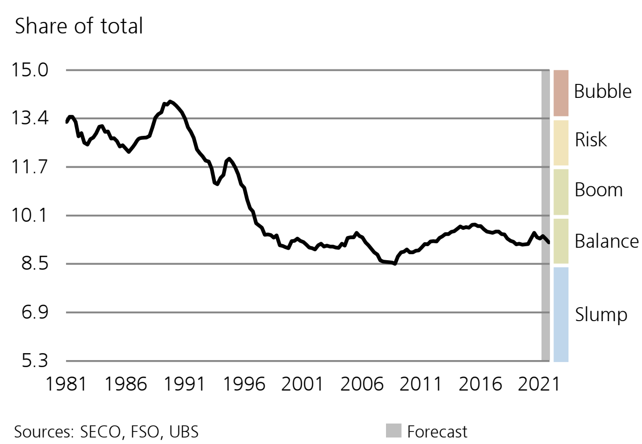
The indicator shows whether the price behavior of the owner-occupied housing market is supported by a change in household income. A decoupling of prices from average household income can be interpreted as a sign of interest rate risks.



Sources: SNB, FSO, UBS

Construction relative to gross domestic product (GDP)

The construction sector gaining weighting within the national economy can signal an overheating of the real estate market.



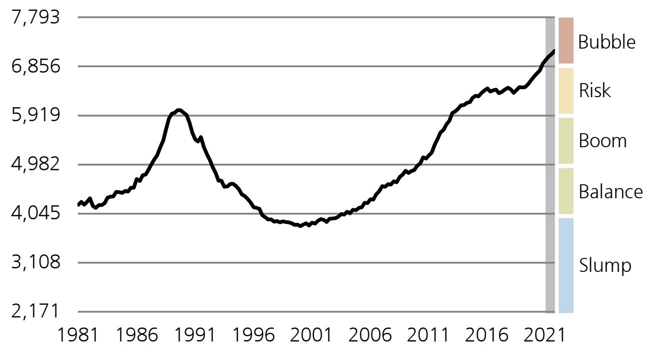
Sources: SECO, FSO, UBS

Sub-indexes of the UBS Swiss Real Estate Bubble Index

Home prices relative to consumer prices

Over the long term, owner-occupied housing prices are likely to relate to construction costs and general inflation. A sharp and lasting increase in inflation-adjusted owner-occupied housing prices is thus a warning signal for a possible correction.

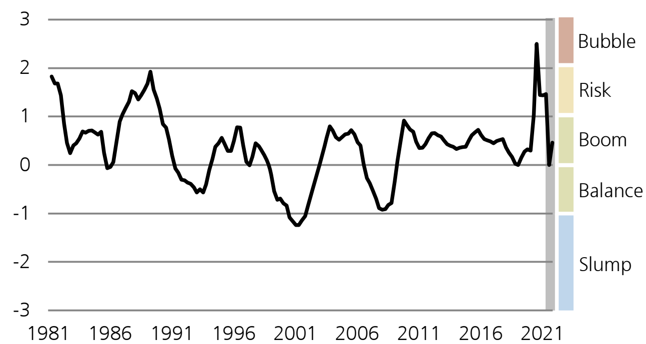
Real owner-occupied housing price index (CHF/m2)



Sources: SNB, FSO, UBS
Forecast

Mortgage volume relative to disposable income of private households
Any sharp growth in mortgage debt is a clear indication of the owner-occupied housing market overheating. If interest rates rise or owner-occupied housing prices correct, high household debt increases the negative consequences for the national economy.

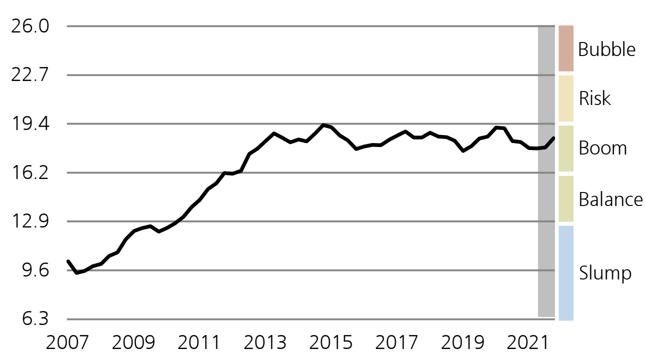
Mortgages of private households relative to income (trend-adjusted, standardized)



Sources: SNB, FSO, UBS
Forecast

Credit applications for residential real estate not intended for self-occupancy (UBS clients)
High demand for residential property for the purpose of leasing (buy-to-let) indicates greater speculative demand.

Share of total



Source: UBS
Forecast

Regional risk map

The regional risk map shows the regions with the most pronounced risks in the housing market. Regionally, three types of risks can be distinguished. There has been an increase in fundamental risk – decoupling home prices from household income and rental price levels. In addition, the boom in the housing market in some regions has caused a sharp rise in the risk of overheating – a significant overhang in demand causes prices to overshoot. There are also regions where liquidity risk – a lot of supply with little demand making it difficult to sell – is elevated. This map replaces the previous regional risk map and is updated every six months.

Risk regions in the Swiss residential real estate market

- Fundamental risk
- Overheating risk
- Liquidity risk

Source: UBS

Appendix

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