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Investment Research

UBS Swiss Real Estate Bubble Index

Swiss real estate market

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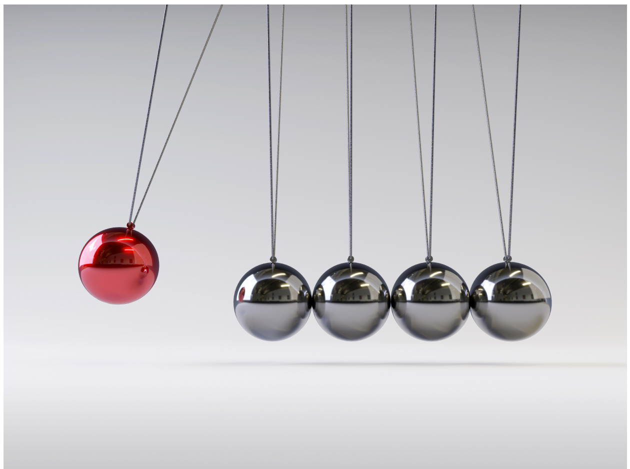
- The *UBS Swiss Real Estate Bubble Index* fell minimally in the third quarter of 2023 from 1.43 to 1.41 points. The market for owner-occupied homes remains relatively overvalued compared to its history.
- A material increase in the price for owner-occupied homes met a stagnant economy. As a result, the ratio of owner-occupied home prices to incomes and consumer prices continued to climb. Despite a slower growth in mortgages, the rise in household leverage added to the risks on the owner-occupied housing market.
- The lower index level was primarily due to a clear increase in rents. Accordingly, the price-to-rent sub-index fell sharply.



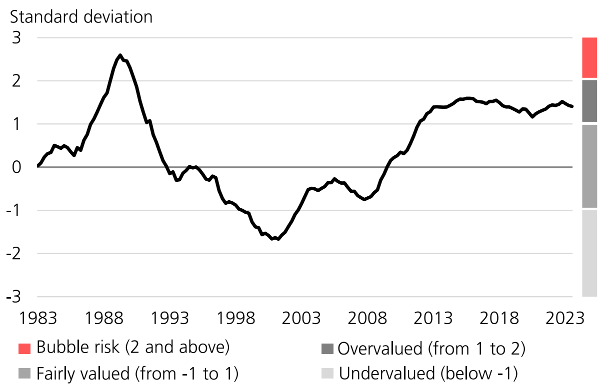
Source: Shutterstock

Development of market drivers: The 0.7% price increase for residential property in the third quarter 2023 was comparable with previous quarters. Asking rents, by contrast, jumped 2.8%. Conversely, in view of the weak economy, income per household dipped in the past quarter. Nominal construction investment also fell slightly quarter-over-quarter. Moreover, higher financing costs continued to weigh on the growth of outstanding mortgages, which have now practically dropped to the low point of the 1990s.

Statement of risk: The *UBS Swiss Real Estate Bubble Index* is currently significantly lower than during the real estate bubble at the beginning of the 1990s, but nevertheless still suggests clear overvaluation of the local owner-occupied housing market. Owner-occupied housing prices are still proving resistant in the face of increasing financing costs. An ongoing decline in and generally low new construction activity make a considerable price correction unlikely in the near future, in our view. However, falling transaction volumes, low growth on the mortgage market, and supply growth indicate decreasing demand for owner-occupied homes. We believe the imbalances on the market will decline in the medium term due to increasing rents.

UBS Swiss Real Estate Bubble Index

3rd quarter 2023



Source: UBS

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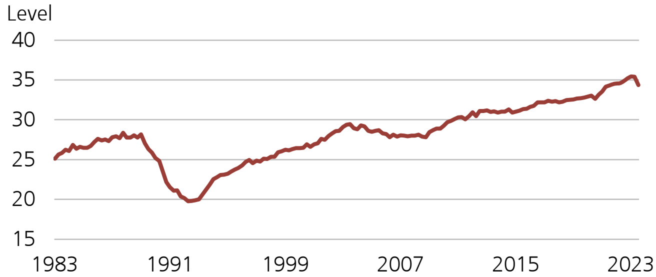
Sub-indexes

Home prices relative to annual rents

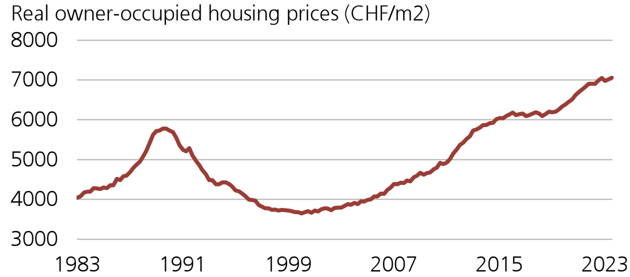
An above-average price-to-rent ratio indicates a high dependency on sustained low interest rates or implies expectations of future price increases.



Sources: Wüest Partner, IAZI, FPRE, FSO, UBS

Home prices relative to consumer prices

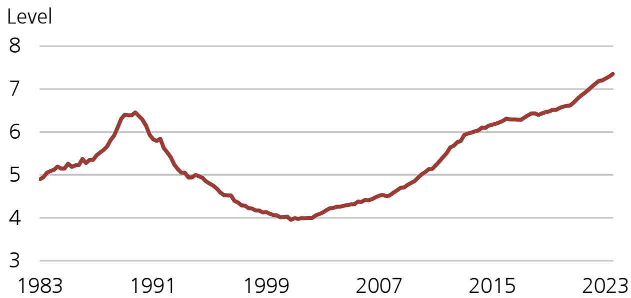
If owner-occupied home prices rise faster than construction costs and general inflation for a long time, this can be a warning of a possible correction.



Sources: Wüest Partner, IAZI, FPRE, FSO, UBS

Home prices relative to household incomes

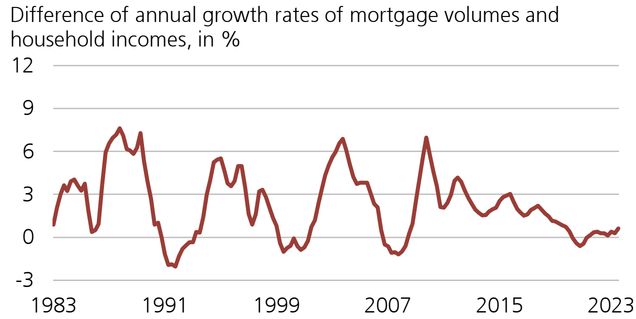
If the price development in the market for owner-occupied homes is not supported by a change in household incomes, this can be interpreted as a signal for interest rate risks.



Sources: Wüest Partner, IAZI, FPRE, FSO, UBS

Mortgage volumes relative to household incomes

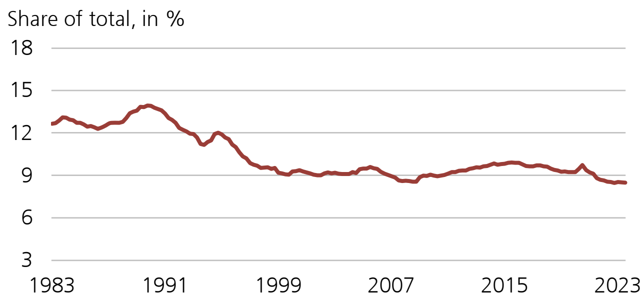
An acceleration in household debt that is not accompanied by income growth is a signal of an overheating of the real estate market.



Sources: SNB, FSO, UBS

Construction relative to gross domestic product (GDP)

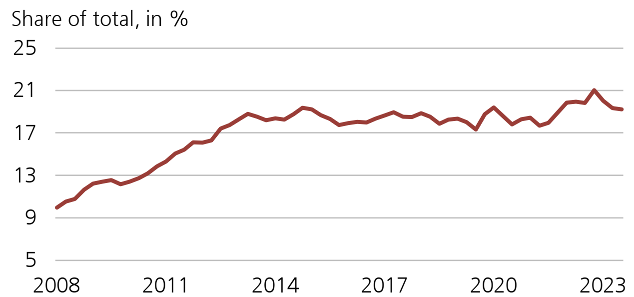
If the construction sector gains weight within the national economy, this can imply an overheating of the real estate market.



Sources: SECO, FSO, UBS

Credit applications for buy-to-let properties

High demand for residential property for the purpose of leasing (buy-to-let) indicates greater speculative demand.



Sources: SNB, UBS

Regional risk map

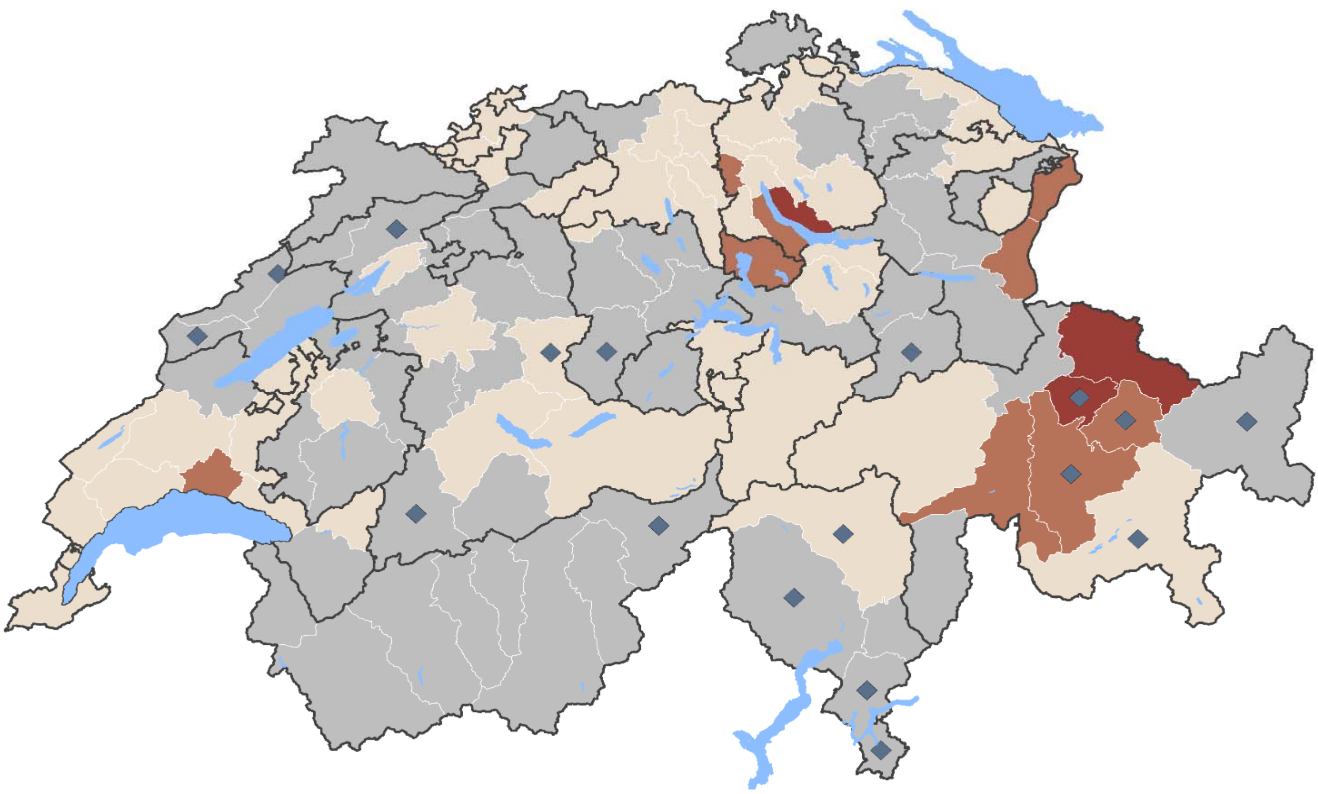
Assessment
The risk map shows the short- to medium-term risk of overheating. The market is (severely) overheated at Lake Zurich, in parts of Graubünden, in the St. Galler Rhine valley, and in the Lausanne region. In these regions, purchase prices have risen significantly faster than market rents over the past five years. This development is not sustainable, in our view, especially against the backdrop of rising financing costs. By contrast, this relative risk has fallen in Zurich and Geneva over the past year from "high" to "slightly elevated." In the Geneva region, this decline was driven by prices stagnating in the previous quarters. The sharply rising rents in Zurich have also put the price development for owner-occupied housing into perspective.

Remark
According to the UBS Global Real Estate Bubble Index 2023, Zurich is in the bubble risk zone. The risk there is considered in a longer-term context , and calculated on the basis of various indicators. However, sharply rising rents have also led to a decline in the price-to-rent ratio and, as a result, to a falling risk assessment.

Method
The regional analysis is based on how the local price-to-rent ratio has changed over the past five years. In addition, regions with falling population numbers (last three years) are marked.

The development in rents shows the situation on the housing market. The price-to-rent ratio reflects the interest rate level and expectations about future increases in rental prices. If there is a strong, above-average increase in this ratio compared to other regions, this can indicate overheating in the local market for owner-occupied homes. Independent of this, a decreasing population represents a risk for real estate demand.

Regional risk map



Relative risk assessment: low, slightly elevated, elevated, high

Regions with falling population numbers

Sources: Wüest Partner, FSO, UBS

Appendix

Index calculation

The UBS Swiss Real Estate Bubble Index represents the weighted average of six standardized sub-indexes using principal component analysis. The index shows the discrepancy, measured in standard deviations, from the mean normalized to zero. The index uses the following classification: Undervalued (below –1), fairly valued (from –1 to below 1), overvalued (from 1 to below 2) and bubble risk (2 and above).

Comment on the adjustment of the index history

The numbers are standardized (recursively) using the data available up to the relevant point in time. For example, the index value in the first quarter of 2015 is calculated using data from 1980 up to the first quarter of 2015. All index values up to and including 2010 are standardized (non-recursively) with data from 1980 to 2010 to ensure there are sufficient data points. That means that the published index values now reflect the imbalances from the perspective of the relevant quarter.

Deviations from the previously published index values can be explained by data revisions.

UBS Swiss Real Estate Bubble Index

Data series since 2017

Period	Index	Trend*
2017-1	1.47	↘
2017-2	1.52	↗
2017-3	1.52	→
2017-4	1.55	↗
2018-1	1.50	↘
2018-2	1.43	↘
2018-3	1.40	↘
2018-4	1.40	→
2019-1	1.36	↘
2019-2	1.32	↘
2019-3	1.28	↘
2019-4	1.35	↗
2020-1	1.34	↘
2020-2	1.25	↘
2020-3	1.16	↘
2020-4	1.24	↗
2021-1	1.28	↗
2021-2	1.32	↗
2021-3	1.35	↗
2021-4	1.41	↗
2022-1	1.44	↗
2022-2	1.43	↘
2022-3	1.46	↗
2022-4	1.52	↗
2023-1	1.47	↘
2023-2	1.43	↘
2023-3	1.41	↘

Source: UBS.

*Compared to the previous quarter

Appendix

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