UBS Swiss Real Estate Bubble Index 1Q. 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 1.80 points in the first quarter of 2021, driven primarily by an acceleration of price momentum in the residential housing market.
- After the distortions caused by the coronavirus have subsided, the risks on the residential housing market are likely to be significantly higher than before the pandemic.

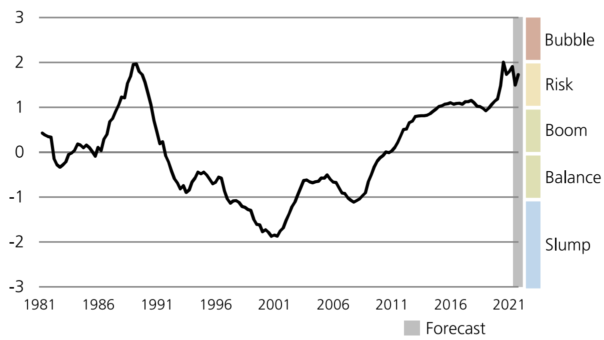
Source: Mauro Mellone, UBS

The *UBS Swiss Real Estate Bubble Index* rose slightly from 1.73 to 1.80 points in the first quarter of 2021, remaining in the risk zone. The increase was due to accelerated price momentum in the residential housing market. Prices rose by 4.4 percent in the first quarter of 2021 compared to the same quarter of the previous year; the strongest increase in eight years. At the same time, rents continue their downward trend and are currently 2.5 percent below their previous year's level. This means that the decoupling of home prices from rents continues to proceed, thus exacerbating the dependence on the low interest rate environment.

Threat of overheating

Strong economic recovery triggered a rise in household incomes at the end of last year. For this reason, as well as thanks to relatively stable mortgage growth and unchanged buy-to-let demand, the bubble risk has not increased more strongly. However, the forecasts do not give us reason to breathe a sigh of relief.

UBS Swiss Real Estate Bubble Index



Source: 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 than 1), Risk (from 1 to less than 2) and Bubble (2 and upwards).

For the year as a whole, significant price hikes are also to be expected while rents continue to fall. The economic recovery in the second half of the current year should prevent risks from rising too rapidly. We currently expect an index level of 1.73 for the final quarter of 2021, slightly below the current level. This forecast of the year-end value was introduced due to the current volatility of the data (see comment below). However, once the dust kicked up by the pandemic has settled, the imbalances in the residential housing market will be severely higher than before the crisis.

Risk map for residential housing

The previous risk map was replaced by the semi-annual *Residential Housing Market Risk Map* report. Regional risks are divided into fundamental risks (home prices are decoupled from household income and rental price levels), overheating risk (significant excess demand causes prices to overshoot) and liquidity risk (high supply with low demand makes sales difficult). Currently, the fundamental and overheating risks are highest in the major centers of Zurich, Basel, Geneva and Lausanne. Liquidity risks exist in parts of Valais, Ticino and the canton of Neuchâtel.

Comment: Restrictions due to corona continue to cause considerable volatility in the economic performance. This leads 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, also present the expected development 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	1.12	Decrease
	Quarter 4	1.15	Increase
2018	Quarter 1	1.10	Decrease
	Quarter 2	1.02	Decrease
	Quarter 3	1.02	Unchanged
	Quarter 4	0.98	Decrease
2019	Quarter 1	0.92	Decrease
	Quarter 2	0.98	Increase
	Quarter 3	1.06	Increase
	Quarter 4	1.13	Increase
2020	Quarter 1	1.19	Increase
	Quarter 2	1.48	Increase
	Quarter 3	2.01	Increase
	Quarter 4	1.73	Decrease
2021	Quarter 1	1.80	Increase
	Quarter 2	1.91	Increase
	Quarter 3	1.49	Decrease
	Quarter 4	1.73	Increase

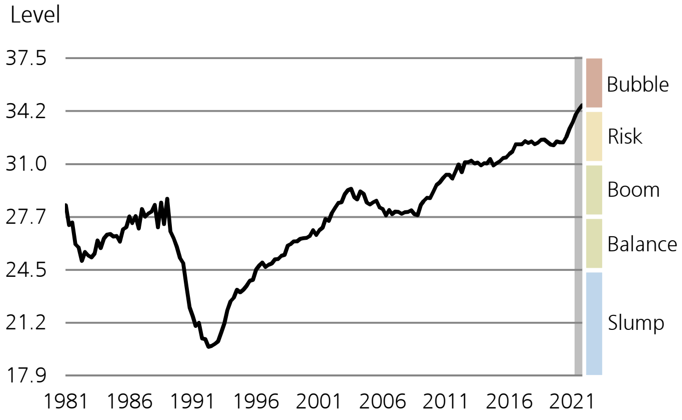
Increase compared to the previous quarter
Decrease compared to the previous quarter
Unchanged
Forecast

Source: UBS

Sub-indexes of the UBS Swiss Real Estate Bubble Index

Home prices to annual rents

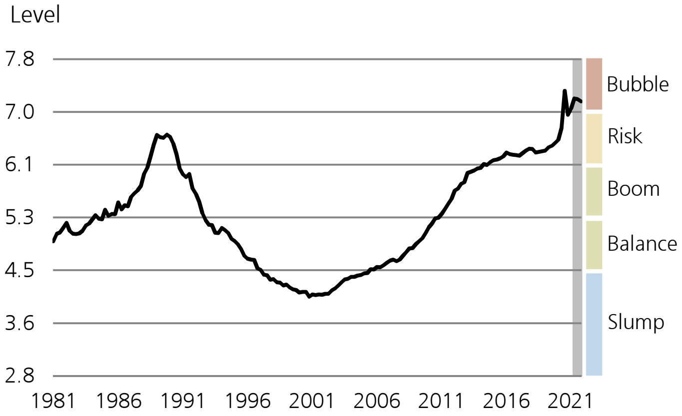
An above-average price-to-rent ratio indicates a high dependency on sustained low interest rates or implies expectations of price increases.



Sources: SNB, UBS

Home prices to household income

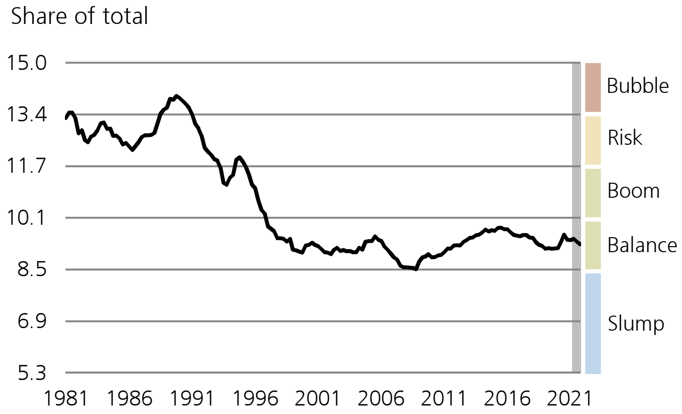
The indicator shows whether the price behavior of the owner-occupied housing market is supported by a change in household income. A decoupling of prices from average household income can be interpreted as a sign of interest rate risks.



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.



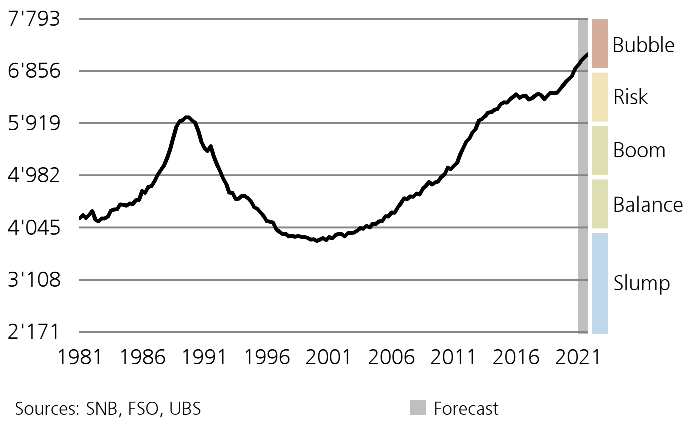
Sources: SECO, FSO, UBS

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)

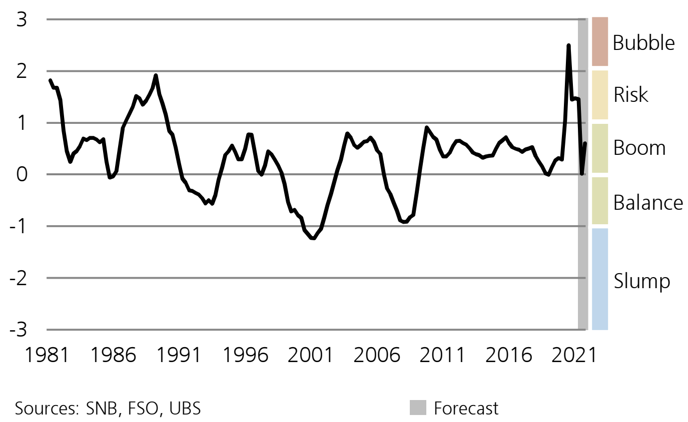


Sources: SNB, FSO, UBS

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)

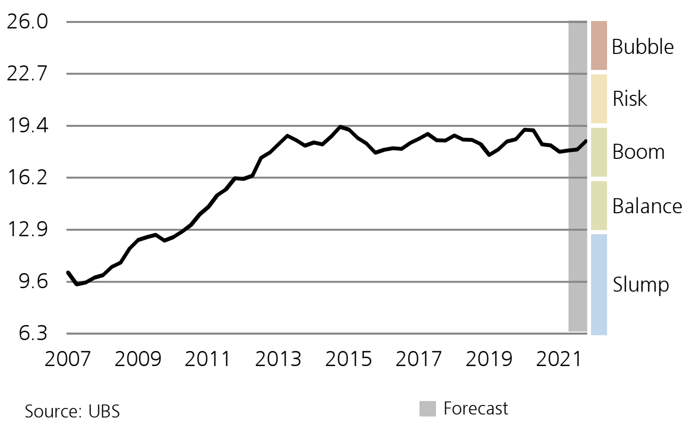


Sources: SNB, FSO, UBS

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

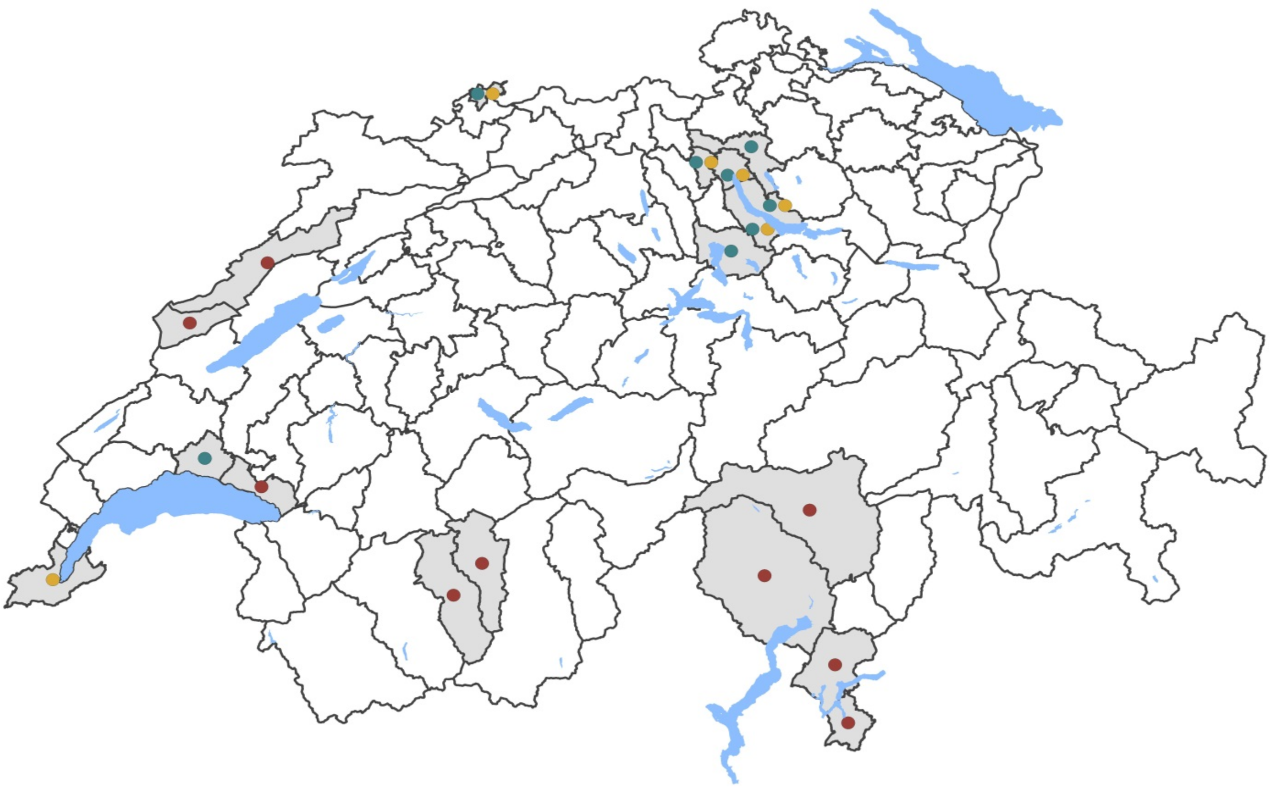


Source: UBS

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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