

Detecting house price bubbles - *UBS Swiss Real Estate Bubble Index*

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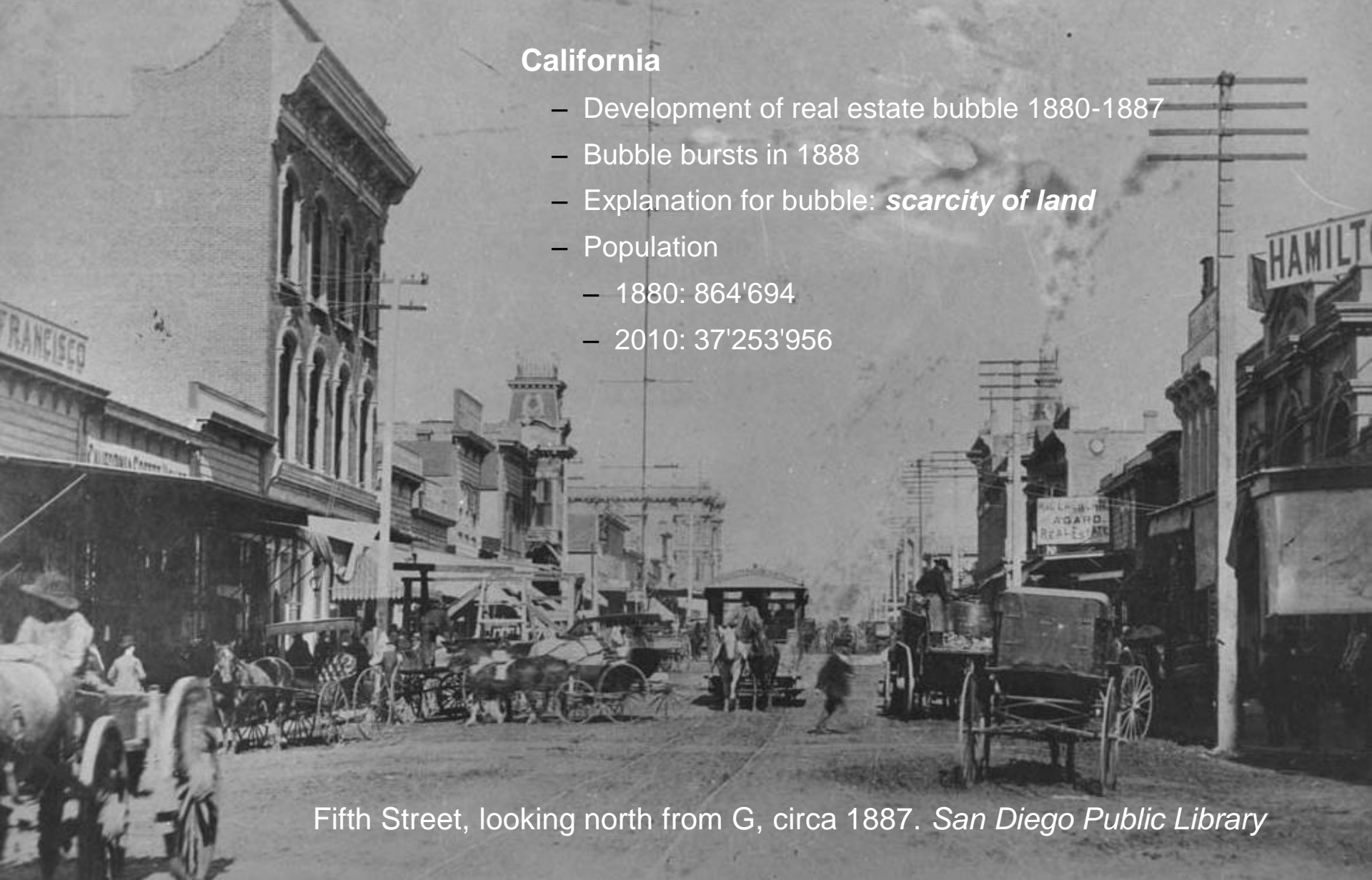
Economist, CIO WM Real Estate Research



Plausible story — *Fairy tale of scarce land*

California

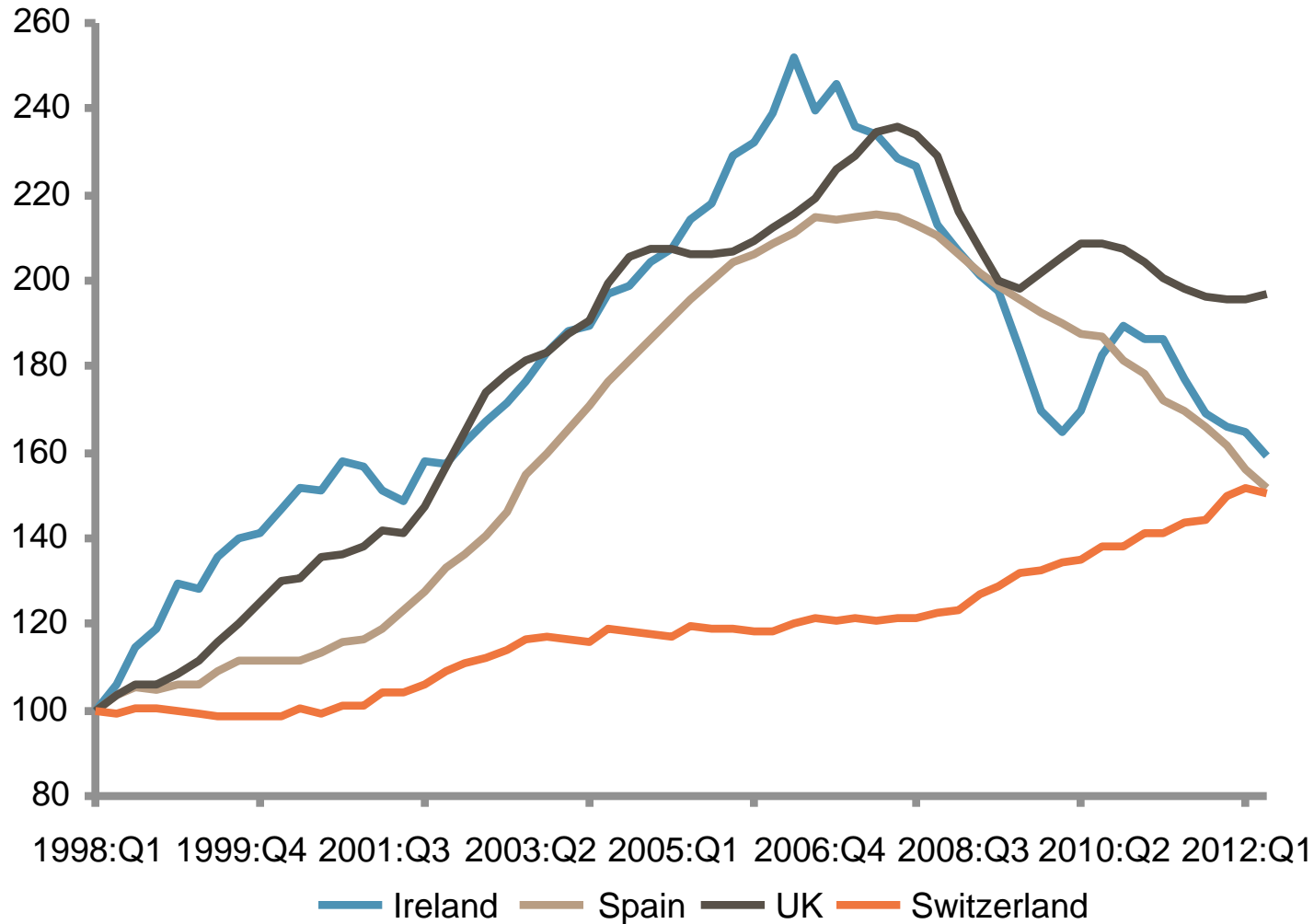
- Development of real estate bubble 1880-1887
- Bubble bursts in 1888
- Explanation for bubble: *scarcity of land*
- Population
 - 1880: 864'694
 - 2010: 37'253'956



Fifth Street, looking north from G, circa 1887. *San Diego Public Library*

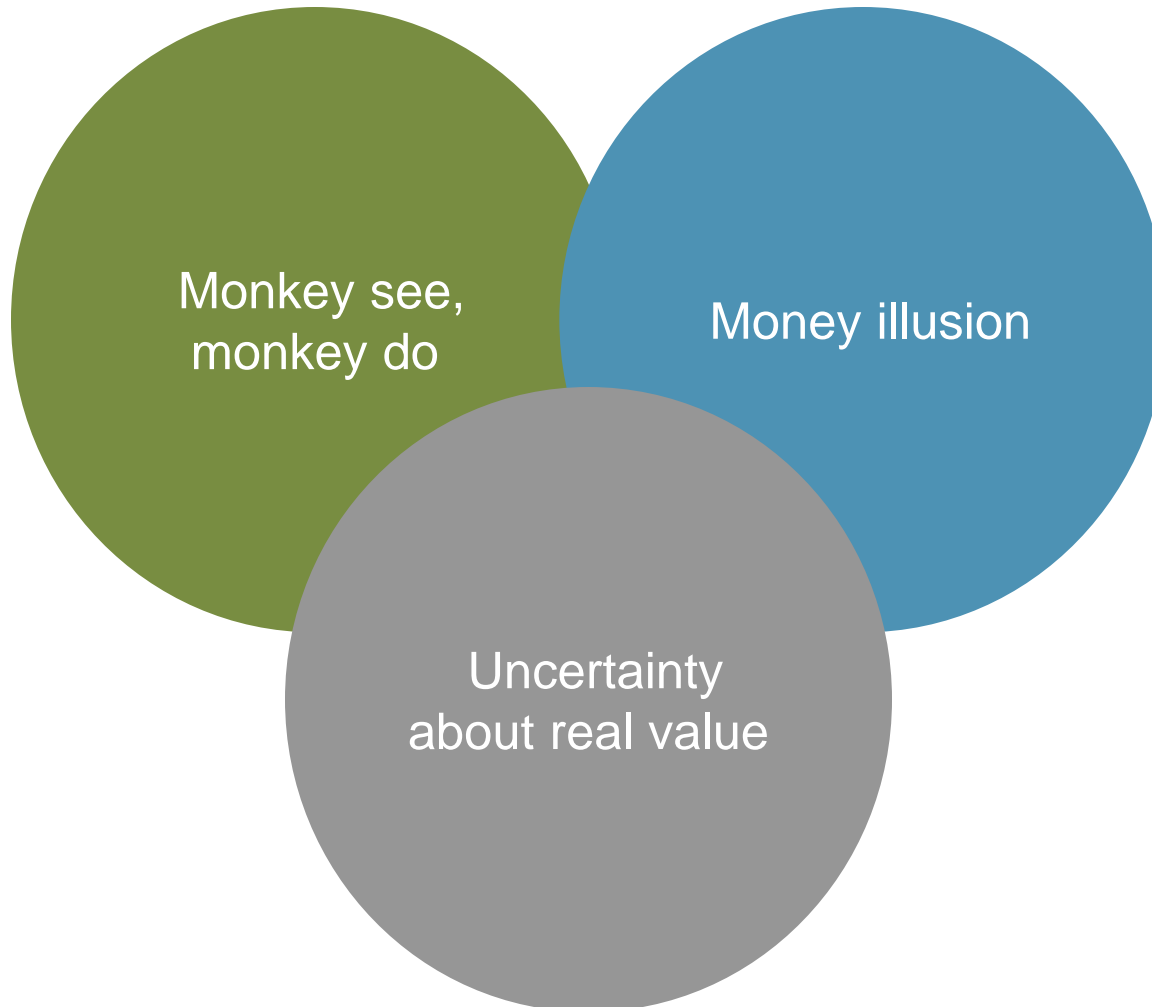
Burst real estate bubbles and Switzerland

Real price indices, year 1998 = 100



How is a real estate bubble *defined*?

A real estate bubble is a deviation of the market price from the fundamental value of an investment driven by ***speculative*** demand.




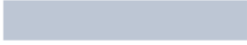
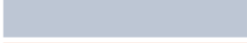


















How a real estate bubble can be *detected*?

A real estate bubble should be not detected by its burst!

1. (Chart) Technical perspective
2. Fundamental perspective
3. Behavioral perspective

Are fundamental analyses *reliable*?

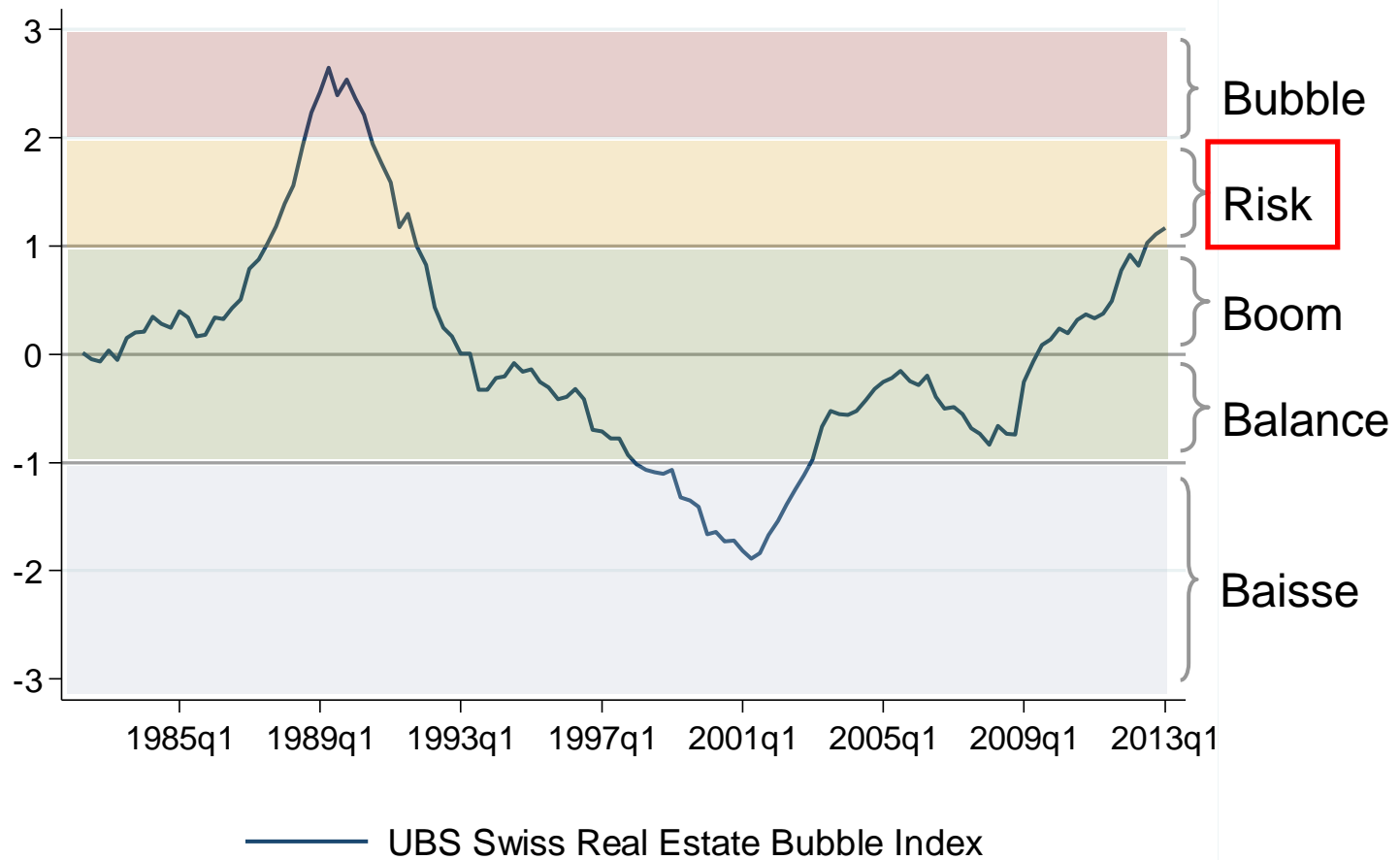
<i>Analysed countries</i>	<i>Assessment in OECD 2005*</i>	<i>Real price development</i>		<i>Ex-post analysis</i>
		<i>till peak</i>	<i>since peak</i>	
USA		8,7%	-25,4%	✗
Japan		-1,1%	-12,1%	✗
Germany		-0,4%	-3,9%	✓
France		20,9%	-3,5%	✓
Italy		9,4%	-17,0%	✗
UK		13,8%	-16,5%	✓
Canada		46,6%	0,0%	✓
Australia		25,3%	-8,3%	✗
Denmark		33,6%	-28,5%	✗
Finland		14,7%	-5,5%	✓
Ireland		21,6%	-36,9%	✓
Korea		13,8%	-1,3%	✓
Netherlands		7,9%	-16,4%	✓
Norway		41,0%	0,0%	✗
New Zealand		23,3%	-12,3%	✓
Spain		12,7%	-29,5%	✓
Sweden		34,2%	-5,7%	✗
Switzerland		25,0%	0,0%	✓
Significantly overvalued				
Slightly overvalued			Miss	✗
Not overvalued			Hit	✓

Indicator system of the UBS Swiss Real Estate Bubble Index

Transparent and clear methodology

- (Chart) Technical perspective
 - Owner-occupied housing prices in consumer prices
- Fundamental perspective
 - Ratio owner-occupied housing prices and rental costs
 - Ratio owner-occupied housing prices and household income
- Behavioral perspective
 - Loan applications (UBS) for buy-to-let properties
- Further indicators
 - Outstanding mortgages to income
 - Construction volume to GDP

UBS Swiss Real Estate Bubble Index – 1. Quarter 2013



Regulatory measures to reduce mortgage risks

- **New (qualitative) guidelines for mortgage business (SBVg, as at 1.1.2012)**
- **Guidelines regarding minimum requirements for mortgage lending (SBVg, 1.7.2012)**
 1. Minimum share of own equity on collateral value of 10 per cent, which is not allowed to come from pension funds savings.
 2. The mortgage debt must be reduced in at least 20 years to 2/3 of the collateral value.
- **New capital adequacy ordinance (as at 1.1.2013)**
- **Introduction of countercyclical capital buffer as at October 2013**
 1. Banks be obliged to hold a countercyclical capital buffer amounting to 1% of their risk-weighted, direct or indirect mortgage-backed positions secured by residential property in Switzerland.
 2. The banking industry will need to hold additional equity capital in the amount of CHF 2 billion. At a constant return on equity, new mortgages will become more expensive by 3-5 basis points.
 3. The countercyclical capital buffer is still clearly below the suggestion in the ordinance which proposes that the capital buffer can amount to a maximum of 2.5% of banks' risk-weighted positions in Switzerland.

Conclusion

- The *UBS Swiss Real Estate Bubble Index* has become the *Benchmark* for the market evaluation in Switzerland
- The index meets with *media interest* national and international
- *Transparent* and *clear* methodology are the base for the success of the product
- Used intensely by internal and external *risik boards* and *customer service*
- The *regional risk map* which is linked with the index is used internally and externally (e.g. by pension funds) for portfolio management

Questions?



**Thank you for
your attention!**

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