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Chief Investment Office GWM
Investment Research

UBS Swiss Real Estate Bubble Index

Swiss real estate market

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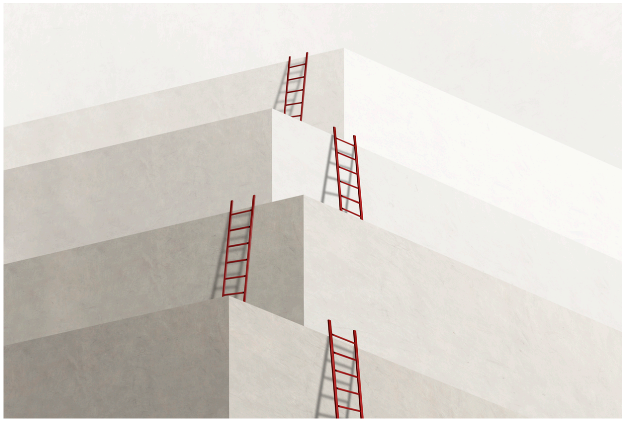
- The *UBS Swiss Real Estate Bubble Index* fell in the second quarter of 2024, and continues to point toward a moderate risk of a bubble in residential property.
- In comparison with last year, the risk of a real estate bubble has declined from all four risk perspectives. Falling occupancy costs as a result of SNB policy rate cuts along with low growth in mortgage volumes are the biggest factors behind the decline. Price growth has also weakened further.



Source: iStock

The *UBS Swiss Real Estate Bubble Index* continued to drop in the second quarter of 2024 and currently stands at 0.74 index points. This means that the risk of a real estate bubble is classed as "moderate". However, the index is significantly lower than it was during the real estate bubble in the early 1990s.

Market trends in the second quarter of 2024

Owner-occupied housing prices recorded an increase of 0.4% in the second quarter of 2024, which is the lowest quarter over quarter rise in prices since the beginning of 2019. Year over year, this meant that owner-occupied homes increased in price by 2.7%. Adjusted for inflation, prices were 1.4% higher than in the summer of 2023.

By contrast, rents continued to rise at a brisk pace. In the second quarter of 2024 quoted rents went up by 1.2%, making them 6.4% higher than they were a year before. Existing rents also recorded an above-average year over year increase of 2.7%.

Outlook: We expect prices for owner-occupied homes to continue to rise over the next few months. Overall, owner-occupied properties are likely to rise in price this year by about 2%. Next year, we expect price momentum to pick up. Besides falling mortgage interest rates, the sharp rise in rents will also have a positive impact on demand in the market for owner-occupied homes.

UBS Swiss Real Estate Bubble Index

2nd quarter 2024, in standard deviations. Depending on the current index value, the real estate bubble risk is divided into the following four categories: low (below 0), moderate (between 0 and 1), elevated (between 1 and 2), and acute (above 2).

Source: UBS

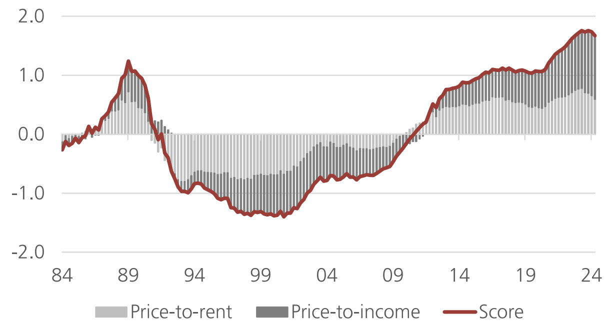
Risk of a real estate bubble from four perspectives

Existing imbalances and risks in the market for owner-occupied properties are viewed from four different perspectives.

Foundation
Score: 1.73 (previous quarter 1.80), Risk: elevated
Indicators: price-to-rent and price-to-income ratios
The deviation in owner-occupied property prices from household incomes and rents is an indicator of how far prices might fall, as well as a sign of prices being inflated. These two variables are brought together in the overarching term "foundation."

Development: In the first half of 2024 rents rose more than twice as fast as owner-occupied property prices, causing the price-rent ratio to drop. The ratio between purchase prices and incomes, on the other hand, has continued to rise slightly so far in 2024. Weak economic growth is acting as a drag on increases in income per household.

Foundation
2nd quarter 2024, in standard deviations

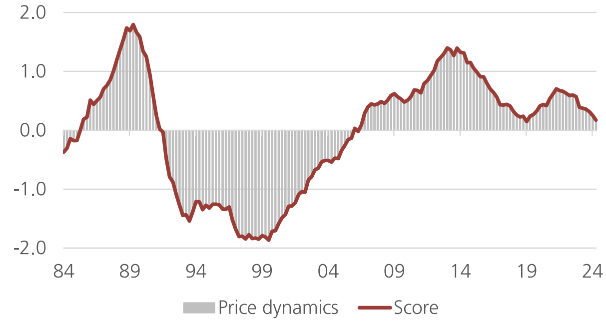


Source: UBS

Dynamics
Score: 0.17 (previous quarter 0.25), Risk: moderate
Indicator: Real rate of price change over three and 10 years
Price bubbles are accompanied by an unusually large increase in real property prices. This is a technical way of looking at it, which does not take account of the cause of the change in prices.

Development: The momentum of the price rises in the owner-occupied property market continues to slow. Averaged over three years real prices have increased by an annualized 1.7%, which is only slightly higher than the long-term mean of 1.5%. Averaged over 10 years, the rate of growth has likewise been a little below the 2% mark.

Dynamics
2nd quarter 2024, in standard deviations

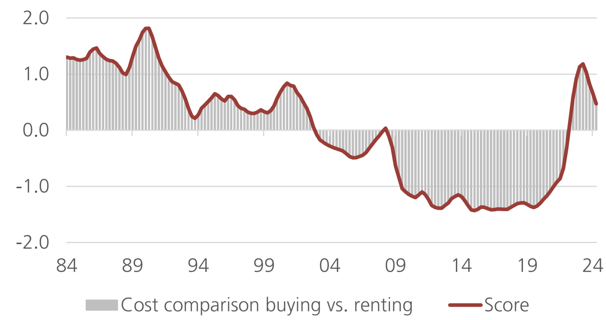


Source: UBS

Cost
Score: 0.47 (previous quarter 0.65), Risk: moderate
Indicator: Cost comparison of purchase and rent
The occupancy costs when purchasing your own home (cost of capital, repayments, upkeep) and the rental costs for a comparable property should roughly balance out over the long term. The risk of a correction is elevated if the occupancy costs for owner-occupied properties are above average compared to rental properties.

Development: Falling mortgage interest rates resulting from policy rate cuts along with rising rents have narrowed the premium to be paid for an owner-occupied property compared to a rental property. On average across the market this premium is only in the low single-digit percentage range, putting it well below its high point in mid-2023 when it stood at around 15%.

Cost
2nd quarter 2024, in standard deviations



Source: UBS

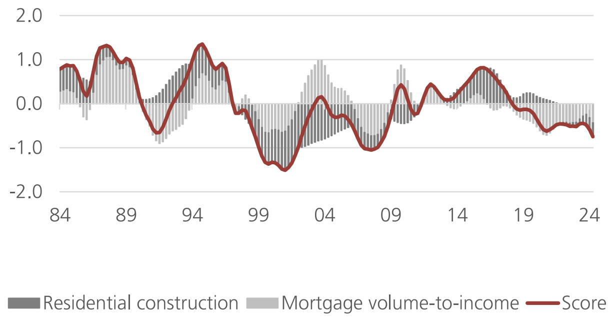
Environment

Score: -0.81 (previous quarter -0.54), Risk: low
Indicators: mortgage volume-to-income and residential construction

Real estate bubbles generally go hand in hand with a boom in household borrowing. At the same time construction activity is often higher, which makes the economic crisis after the end of the boom even worse.

Development: The growth in the volume of outstanding mortgages for private households has bottomed out, and showed a marginally sharper rise in the second quarter of 2024 at 1.7% year over year. On the other hand, the net increase in the housing stock continued to fall.

Environment
2nd quarter 2024, in standard deviations



Source: UBS

Risk contributions

The current decline in the *UBS Swiss Real Estate Bubble Index* has been broadly based. The risk of a real estate bubble has fallen year over year from all four perspectives.

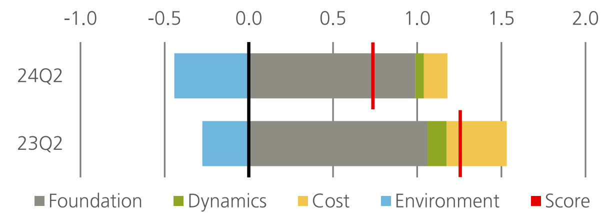
Development over the past two years
Index value and scores for the four perspectives, in standard deviations

	Index	Foundation	Dynamics	Cost	Environment
2022 Q3	**1.06**	1.68	0.60	0.59	-0.40
2022 Q4	**1.18**	1.73	0.57	0.92	-0.39
2023 Q1	**1.20**	1.78	0.39	1.13	-0.39
2023 Q2	**1.26**	1.82	0.38	1.18	-0.29
2023 Q3	**1.19**	1.79	0.36	1.03	-0.27
2023 Q4	**1.10**	1.82	0.32	0.82	-0.33
2024 Q1	**0.95**	1.80	0.25	0.65	-0.54
2024 Q2	**0.74**	1.73	0.17	0.47	-0.81

Source: UBS

Nonetheless, the analysis shows that the risk of a real estate bubble remains high with regard to the fundamental factors of rents and incomes. However, the risk of overheating has decreased with weaker price momentum. Falling interest rates and the moderate level of relative occupancy costs do not make for a price correction. Low demand for mortgages overall and a continued contraction in the number of new properties being built also clearly work against a price bubble.

Risk contributions
In standard deviations



Source: UBS

Regional analysis

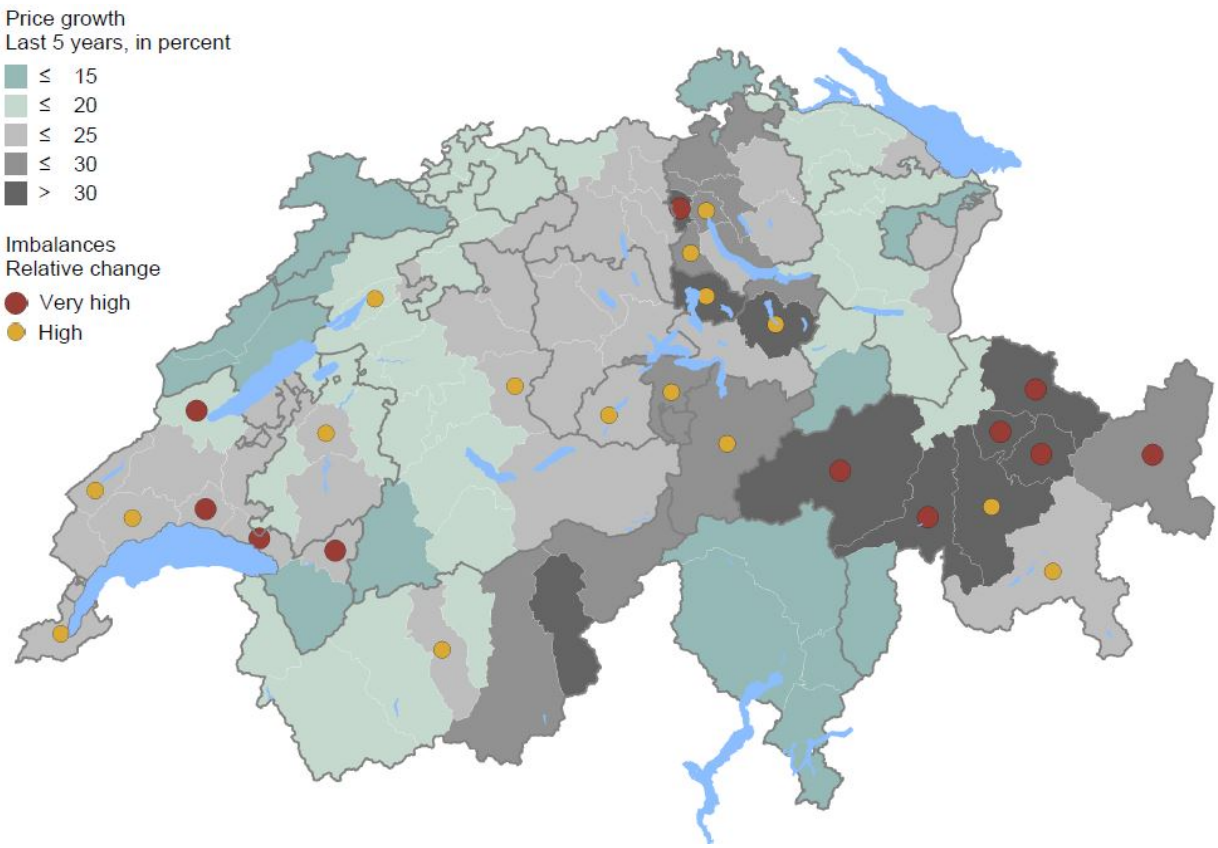
Indicator: The map shows price trends over the past five years for all 106 economic regions in Switzerland as well as an indication of regional risk based on the change in the price-to-income and price-to-rent ratios (foundation perspective).

Development

- A sharp increase in imbalances can be seen as a result of the boom in second homes in the tourist areas in Graubünden.
- The price-to-income ratio has shown a marked deterioration since the start of 2019 in the cities of Zurich and Lausanne in particular, as well as in Geneva. In the regions bordering Lake Geneva this also applies to the price-to-rent ratio.
- Apart from the Limmat Valley region, there has not been a very large increase in imbalances in the market for primary homes in German-speaking Switzerland, as the ratio between purchase prices and rents has registered a below-average increase almost across the board in these regions. Zug is the exception here, and it is also the area with the fastest increase in prices.

Regional imbalances

Development since 1st quarter 2019 (five years)



Source: UBS. Imbalances: Very high: change in price-income and price-rent ratios greater than in 90% of regions. High: change in price-income and price-rent ratios greater than in 75% of regions.

Methodology

The *UBS Swiss Real Estate Bubble Index* is a model based on sub-indices. The risk of a real estate bubble, i.e. the risk of a serious price correction for owner-occupied homes, is viewed from the following four perspectives.

Fundamentals
The sub-indicators *price-to-income* and *price-to-rent ratios* reflect the potential drop in owner-occupied property prices in the event of very sharp rises in interest rates or a deterioration in the economic environment.

Momentum
The purchase prices to consumer prices sub-indicator feeds into the model as a rate of change. High *real price increases* are more or less a necessary condition for a real estate bubble.

Costs
The *occupancy cost comparison* between an owner-occupied home and a comparable rental property shows the current incentive for buying a home to live in or to rent out.

Environment
The systemic risk of oversupply in the housing market and of excessive construction activity is estimated based on the effective *net increase in housing* and the number of housing units granted planning permission. A second systemic indicator used is the *growth in mortgage debt* on the part of households as a ratio of the growth in household incomes.

Calculation
The real estate bubble index is made up of a total of six standardized sub-indices with equal weighting. The sub-indices in the environment category are standardized on a rolling basis over a period of 25 years in order to take account of structural changes in the economy. Other sub-indices are standardized with a long-term average.

Appendix

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