Berne, 28 February 2018

Basel III countercyclical capital buffer

Stance of the Basel III countercyclical capital buffer in Switzerland

- The Basel III countercyclical capital buffer (CCyB) in Switzerland remains at 0%[1].
- The Swiss sectoral CCyB targeted at mortgage loans financing residential property located in Switzerland remains at 2% as decided and communicated by the Federal Council in January 2014. Mandatory reciprocity as foreseen in Basel III does not apply to the Swiss sectoral CCyB requirements.
- The situation on the Swiss credit and real estate markets will be reassessed periodically. Any adjustments to either the sectoral CCyB or the Basel III CCyB will be communicated to the public.

Background

- In June 2012, a countercyclical capital buffer (CCyB) was introduced into Swiss legislation. One important characteristic of the Swiss CCyB framework is that it can be applied on a broad basis – consistent with the Basel III rules – or it can target specific segments of the credit market. In February 2013, a sectoral CCyB targeting residential real estate situated in Switzerland was activated and set at a level of 1%[2] of relevant risk-weighted positions. It

[1] In the Ordinance on Capital Adequacy and Risk Diversification for Banks and Securities Traders the specific provisions relating to the Basel III CCyB are included in Art. 44 and 44a.
[2] Banks were required to meet the CCyB requirements by 30 September 2013.

was subsequently increased to 2%[3] in January 2014. These decisions were taken by the Swiss Federal Council – based on a proposal by the Swiss National Bank.

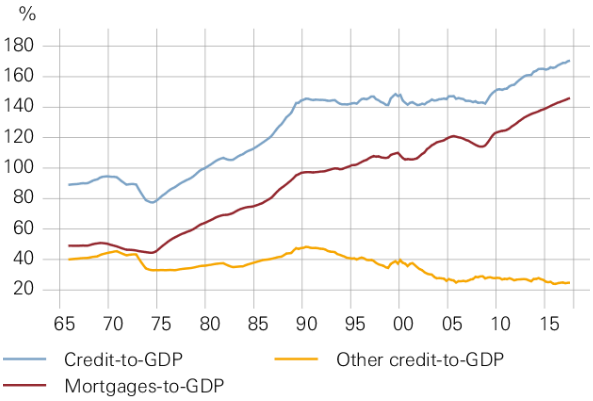
- With the international phase-in of the countercyclical buffer regime having begun in 2016, Swiss authorities are now required to regularly communicate the level of the Basel III CCyB, even if set at 0%.[4]

Motivation for activating / increasing the sectoral CCyB

- Strong growth in both bank credit and real estate prices over the course of several years resulted in the build-up of imbalances on the residential mortgage and real estate markets. By the second half of 2012, Swiss authorities assessed the imbalances to have reached a level that posed a risk to the stability of the banking sector, and hence to the Swiss economy. In response, Swiss authorities introduced several measures. One of the measures, the activation of the sectoral CCyB, was taken in February 2013.
- The observed imbalances have been confined to the residential mortgage and real estate markets. Mortgage volumes[5] relative to GDP have experienced significant growth since 2008 while the level of other credit – relative to GDP – has stagnated or even slightly decreased (cf. chart 1). Similarly, the evolution of real estate prices for both single-family houses and apartments has been distinct from that observed for offices and businesses (cf. chart 2).

CREDIT AGGREGATES-TO-GDP

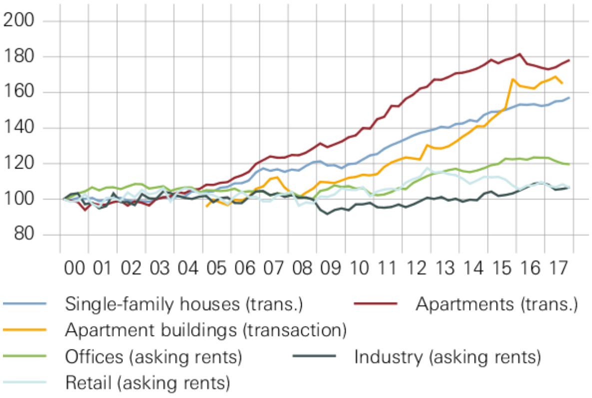
Chart 1



Sources: BFS, SECO, SNB

REAL ESTATE PRICE INDICES

Asking and transaction prices, in real terms, Q1/2000 = 100 Chart 2



Sources: BFS, Wüest Partner

[3] Banks were required to meet the CCyB requirements by 30 June 2014.

[4] http://www.bis.org/publ/bcbs187.htm

[5] At end-2016, around 85% of mortgages were residential mortgages. This share has been very stable over the last couple of years.

- Given the confined nature of observed imbalances, Swiss authorities were of the opinion that the targeted sectoral CCyB is the best suited instrument. It temporarily increases the capital requirements associated with residential mortgage loans while leaving those for other exposures unchanged. This minimizes unintended effects on other credit segments. The significant importance of mortgage loans for banks' business models ensures that an activation of the sectoral CCyB leads to an increase in resilience at the system level. The higher capital requirement and the increase of the relative price of mortgages may further help to 'lean against the wind'.

Developments since the last communication on the Basel III CCyB

- Imbalances on the Swiss mortgage and residential real estate markets persist. They remain confined to the residential mortgage and real estate markets.
- On the mortgage market, volume growth has remained relatively low. However, affordability risks[6] have risen further. Developments on the real estate market are mixed. Transaction prices for single-family houses and apartments suggest that price growth in the owner-occupied segment has started to pick up again after a period of stability. In the residential investment property segment, prices for apartment buildings have continued to grow. Signs of an oversupply are growing in this segment, as brisk construction activity continues against the background of rising vacancy rates.
- Based on these observations, the Swiss authorities are of the view that the sectoral CCyB, which currently amounts to 2%, remains the appropriate measure for tackling observed imbalances. The authorities continue to monitor closely the developments on the credit and real estate markets to assess the need for either an adjustment to the sectoral CCyB or a shift towards the broader based Basel III CCyB.

[6] Measured as the share of new mortgages with high loan-to-income ratios.