Swiss National Bank proposal to increase the countercyclical capital buffer

After consultation with the Swiss Financial Market Supervisory Authority (FINMA), the Swiss National Bank (SNB) has submitted a proposal to the Federal Council, requesting that the sectoral countercyclical capital buffer (CCB) be increased from 1% to 2% of risk-weighted positions secured by residential property situated in Switzerland (cf. appendix). The proposal sets a deadline for compliance with the increased CCB requirements of 30 June 2014. The Federal Council yesterday approved the SNB’s proposal. According to the agreement between the SNB and the Federal Department of Finance, the SNB herewith publishes its proposal together with the main reasons for its assessment.

In the view of the SNB, the imbalances on the Swiss residential mortgage and real estate markets have increased further since the Federal Council activated the CCB in February 2013. Certainly, the activation of the CCB was at least one important factor which motivated several banks – including some major banks – to implement capital measures in 2013, which helped to increase resilience. Moreover, in 2013, the annual nominal growth in both mortgage lending and residential property prices was lower than in the previous year. Nevertheless, growth was still so strong that there was a further increase in imbalances on the mortgage and real estate markets. Consequently, neither the activation of the CCB nor the other measures taken, for example, the revision of the self-regulation rules, were sufficient to avoid the risk of a sharp correction on the mortgage and real estate markets rising further. What is more, in an environment of persistently low interest rates, coupled with banks’ continued appetite for risk, the danger that imbalances will build up even more unless additional countermeasures are taken is considerable.

The increase in the level of the sectoral CCB will result in a further temporary rise in the capital requirements for mortgage loans on residential property in Switzerland. The increase of the CCB therefore helps to maintain, or further increase, the resilience of the banking
sector to a correction in imbalances on the mortgage and real estate markets. Moreover, the increased CCB requirements can counteract a further build-up of these imbalances since they further reduce the attractiveness of providing residential mortgage loans compared to other loans, as well as limiting the overall potential for lending, given the capital currently available.

In its *Financial Stability Report*, the SNB drew attention to the high risks in mortgage lending, particularly in the area of affordability. As a complement to the CCB, discussions are currently taking place between the Federal Department of Finance, FINMA, the SNB and industry representatives with the aim of strengthening the self-regulation rules on mortgage lending. In addition, the SNB will continue to monitor developments on the mortgage and real estate markets closely, and will reassess the need for an adjustment to the CCB on a regular basis.
Appendix:

Formal proposal to increase the countercyclical capital buffer for specific market segments

Under art. 44 of the Ordinance on Capital Adequacy and Risk Diversification for Banks and Securities Traders (Capital Adequacy Ordinance, CAO), the Swiss National Bank (SNB) can submit a proposal to the Federal Council which obliges banks to hold a countercyclical capital buffer (CCB) in the form of Common Equity Tier 1 capital amounting to a maximum of 2.5% of their risk-weighted positions in Switzerland. The SNB submits such a proposal if it becomes necessary to strengthen the resilience of the banking sector against the risks of excessive credit growth, or to combat excessive credit growth. The CCB can be targeted at specific segments of the credit market.

On the basis of art. 44 CAO, and following consultation with the Swiss Financial Market Supervisory Authority (FINMA), the SNB proposes to the Federal Council that:

*the countercyclical capital buffer for specific market segments be increased by 100 basis points and banks be therefore obliged, from 30 June 2014, to hold a countercyclical capital buffer amounting to 2% of their risk-weighted, direct or indirect mortgage-backed positions secured by residential property in Switzerland, as defined by art. 72 CAO.*