Eidgenössische Finanzmarktaufsicht FINMA
Autorité fédérale de surveillance des marchés financiers FINMA
Autorità federale di vigilanza sui mercati finanziari FINMA
Swiss Financial Market Supervisory Authority FINMA

Mortgage market: a focus area for FINMA's supervisory activities

The volume of mortgages in Switzerland is significant and has increased considerably over the years. This poses risks for households, banks and the economy as a whole. FINMA monitors the lending criteria and solvency of supervised institutions.

FINMA has been following developments in the Swiss mortgage market for a number of years. Very low interest rates, rising incomes, immigration and tax incentives all serve to increase the demand for mortgages. Lending volumes are increasing steadily and, relative to the country's gross domestic product, the level of mortgage debt in Switzerland is approaching one of the highest in the world.

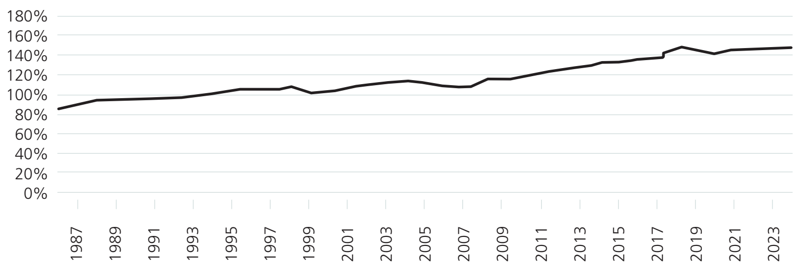
Experience from past crises has shown that problems on the mortgage market can have a rapid and profound impact on financial institutions and the real economy as a whole. In its role as regulator, FINMA therefore places emphasis on sustainable mortgage lending.

FINMA takes supervisory measures

The business and risk policies followed by banks for their lending activities are subject to FINMA supervision. Since 2010, FINMA has also performed its own on-site inspections of mortgage lending practices alongside reviews carried out by audit companies. On an individual basis, FINMA or the audit companies assess how the banks implement the self-regulation requirements of the Swiss Bankers Association, which are recognised as binding by FINMA, in connection with sustainable affordability and property valuation. Moreover, FINMA also regularly reviews the risks involved in the lending portfolios of banks by performing stress tests and conducting data analyses. These tests also allow FINMA to assess whether the banks have sufficient capital to withstand changes in the respective risk drivers (e.g. interest rates, real estate prices) and any resulting losses.

FINMA can take targeted measures to ensure the affordability of mortgages and achieve sustainable lending. FINMA takes action in cases in which it identifies excessive risks or shortcomings in the lending policy. FINMA regularly alerts the institutions' governing bodies to their responsibilities in this area as part of the supervisory dialogue process. FINMA can also impose targeted measures on institutions in order to limit an excessive risk appetite. These measures may include a specific increase in capital requirements, orders to reduce the level of risk or ensuring appropriate and effective credit risk management.

Mortgage volume as a percentage of GDP



Source: SNB

The regulatory framework for the mortgage market

In the case of loan-to-value ratio ceilings, the maximum amount that mortgagors can request is limited on the basis of their available capital. The affordability limits defined by the institutions additionally restrict the maximum amount of the mortgage based on disposable income. The mortgage must be reduced to two thirds of the collateral value through regular payments.

Corresponding requirements are included in the self-regulation of the Swiss Bankers Association and recognised by FINMA as minimum standards. These minimum standards are tightened up by the institutions where necessary. In particular, it is envisaged that the banks will guarantee sustainable financing.

In relation to affordability, for example, FINMA considers the following criteria to be sustainable[1]:

– For the owner-occupied residential property segment: an affordability limit of up to 38% of net income, in conjunction with an imputed mortgage interest rate of 5% of the loan amount and imputed building-related maintenance costs of 0.8% of the collateral value (for new properties)

– For the owner-occupied residential property segment: an ETP (exception to policy) affordability limit of 33% of sustainable gross income together with an imputed mortgage interest rate of 5% of the loan amount and imputed building-related maintenance costs of 0.8% of the collateral value (for new properties)

– For the income-producing real estate segment: an affordability limit of 100% of the sustainable net rental income in conjunction with an imputed mortgage interest rate of 5% of the loan amount and imputed building-related maintenance costs that reflect the age and condition of the property.

– Loan-to-value ratio and amortisation: The property must be valued conservatively. Depending on the risk of the financing, the banks must set lower loan-to-value ratios and higher amortisation rates going beyond the minimum requirements. In the case of income-producing real estate (including "buy to let" financing), for example, the banks' internal loan-to-value and amortisation requirements are stricter since there are increased risks. In the income-producing real estate segment, FINMA's mortgage stress tests show particularly high expected loss rates in the event of severe property crises.

– The criteria above do not represent a comprehensive assessment of sustainable lending. From a supervisory perspective, an overall evaluation of credit risk always considers the characteristics of a financial institution.

FINMA's scope for action

Mortgage lending is influenced by various factors. FINMA can exert a direct influence on mortgage lending and credit risk management at individual banks by auditing the lending process and the corresponding standards, as well as by imposing additional capital requirements and ordering measures to reduce risk. FINMA is also indirectly involved in discussions on capital requirements for mortgage lending, the countercyclical capital buffer and self-regulation in the area of mortgage lending. However, FINMA has only limited powers in these areas.

Measures	Examples	Responsibility lies with
Macroeconomic measures	Fiscal policy (tax policy)	Parliament, government
	Monetary policy (interest rate policy)	Swiss National Bank
Prudential measures	Countercyclical capital buffer	Government
	Capital requirements for mortgage lending for all banks	Government
	Additional capital requirements for individual banks, ordering of risk reduction, auditing of lending process and standards	FINMA
	Self-regulation, e.g. affordability criteria, minimum amortisation, lowest value principle	Industry associations, FINMA

[1] This is based on the assumption of amortisation in accordance with SBA minimum requirements or more conservative amortisation according to the underlying risks.