Jean-Pierre Danthine: Swiss banks from a financial stability perspective

Introductory remarks by Mr Jean-Pierre Danthine, Vice Chairman of the Governing Board of the Swiss National Bank, at the Media News Conference of the Swiss National Bank, Berne, 1 December 2014.

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In my remarks, I would like to look at the situation of the Swiss banks from a financial stability perspective, taking the big banks first and then moving on to a discussion of domestically focused banks.

**Strengthening the resilience of the big banks**

Since the last media news conference, the Swiss big banks have improved their capital situation once again. The Swiss National Bank recognises the considerable progress made in this area as regards both risk-weighted capital ratios and leverage ratios. It is also of the opinion that the strengthening of the big banks' resilience must continue, for the following reasons.

First, risks in the economic and financial environment remain high. In several of the adverse scenarios considered by the SNB, the estimated loss potential for the big banks continues to be substantial relative to their capitalisation. This is also the case when viewed in a historical perspective, as evidenced during the recent financial crisis. Second, while the big banks' risk-weighted capital ratios are above the average for large globally active banks, the same still cannot be said for their leverage ratios.

In this context, the SNB supports the recommendations by the group of experts headed by Professor Brunetti on the evaluation of the “too big to fail” regulatory framework. The report advocates a recalibration of capital requirements in order to ensure that Switzerland is in a leading position internationally in terms of the requirements for both risk-weighted capital ratios and leverage ratios. In particular, the report stresses that leverage ratio requirements for systemically important banks have been increased in several countries compared to the minimum proposed by the Basel Committee. In the SNB’s view, a possible recalibration of capital requirements must reflect the size and concentration of our banking sector. In fact, it is imperative that a lasting solution be found for the “too big to fail” issue in Switzerland.

**Increasing the credibility of model-based risk-weighted assets**

Beyond recalibrating capital requirements, increasing the credibility of the model-based risk-weighted assets (RWA) is essential. This is all the more important as RWA remain a key element of banking regulation.

The Brunetti group of experts, too, considers this to be a prime objective and the issue has also been recognised at international level. The Basel Committee has therefore announced the release of a set of measures for consultation. These measures mainly provide for the revision of the standardised approaches for RWA calculation, the introduction of an RWA floor based on the standardised approaches, as well as greater transparency. The floor is aimed at ensuring that the requirements for banks using the model-based approach remain sufficiently prudent.

In this regard, let us also recall that FINMA – together with the big banks and with the support of the SNB – has conducted a comparison of RWA calculated with the model-based approach and the standardised approach. The SNB suggests that banks consider the possibility of publishing the results of this analysis in appropriate form. In any case, the SNB remains convinced that banks which use the model-based approach for calculating their RWA must continue to improve their transparency with regard to their risks. Considerable
progress has been made already, especially in terms of disclosing changes in RWA broken down by cause. Publishing a parallel calculation of RWA based on the standardised approach would greatly contribute to building trust and market discipline. Enhanced transparency is likely to be a key component of the measures that the Basel Committee will put in consultation.

**Domestically focused commercial banks**

I would now like to turn to the situation of the domestically focused banks. Risks facing these banks are still primarily connected with the mortgage and real estate markets. These risks have largely remained unchanged at a high level over the past six months.

In the last half year, the momentum in the mortgage market slowed, with annual growth in mortgage lending slightly less high than in the previous quarters. The mortgage volume continued to rise more steeply than GDP, but the difference between the two growth rates has become smaller. Furthermore, real estate prices continued to rise but, as in 2013, momentum remained below the levels observed until 2012. Developments still varied widely from one region to the other. Whereas real estate prices in some regions hardly increased or even decreased, other regions continued to register significant price rises.

However, it is still too early for an all-clear. First, the imbalances that have built up since the beginning of the low-interest-rate phase remain at a high level. Second, mortgage interest rates have again dropped to historically low levels in the past few months. And third, there are no broad-based indications of a change in the banks' risk appetite. Mortgage lending growth at the domestically focused banks has also decreased, but is still markedly higher than overall market growth. Moreover, the affordability risk (loan-to-income ratio) in mortgage lending has continued to rise, interest rate risk remains at a historically high level, and interest rate margins have fallen even further, from a level which was already low.

In these exceptional circumstances, banks should ensure that their resilience is high enough to be able to bear the risks taken, even in the event of a marked real estate price correction combined with an interest rate shock. The countercyclical capital buffer plays a significant role in this context by ensuring that banks hold additional capital as a buffer in the current situation. Adding to that, many banks have a surplus of capital with respect to the regulatory requirements. Such surplus capital is especially important under the current circumstances. Banks should therefore maintain these surpluses in future, or should establish and increase them in line with their risk profile.

As before, the SNB will regularly assess whether the countercyclical capital buffer needs to be adjusted due to mortgage and real estate market developments. If the momentum in these markets picks up again, additional measures to limit the affordability risk in mortgage lending should be taken into consideration.