

# **Risk Report 2014Q1**

Published 8 May 2014

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The Risk Report has been prepared by Realkredit Danmark's analysts for information purposes only. Realkredit Danmark will publish an updated Risk Report quarterly.

The Risk Report offers an update on the performance of mortgage collateral supporting mortgage bonds and mortgage covered bonds (covered bonds) issued by Realkredit Danmark.

Contents of the report falls into two parts. The first part contains general market information relevant to the performance of mortgage collateral. The second part contains Realkredit Danmark specific information. Contents of the report are:

## **1 Key Market Indicators**

- House Prices
- Homeowners Equity
- Geographical Dispersion
- Unemployment and Real Wage Growth
- Homeowner Affordability
- Foreclosures
- Danish economic outlook

## **2 Key Collateral Indicators**

- Dispersions Loan to Value Ratios
- Loan to Value Ratios and Borrower Classifications
- Mortgage Collateral Breakdowns — Total, Capital Centre S and Capital Centre T
- Borrower Exposure to Interest Rates
- Arrears and Repossessions
- Over Collateralisation and Capitalisation
- Supplementary Collateral
- Guarantees
- Market Risk Exposures and Liquidity

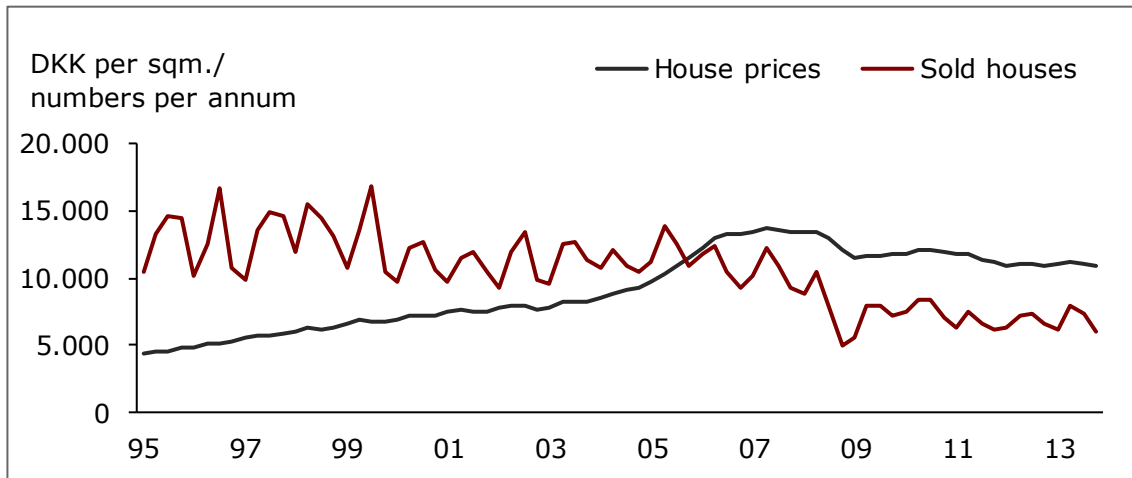
# Key Market Indicators

General Market Information

# 1 House Prices and Homeowners Equity

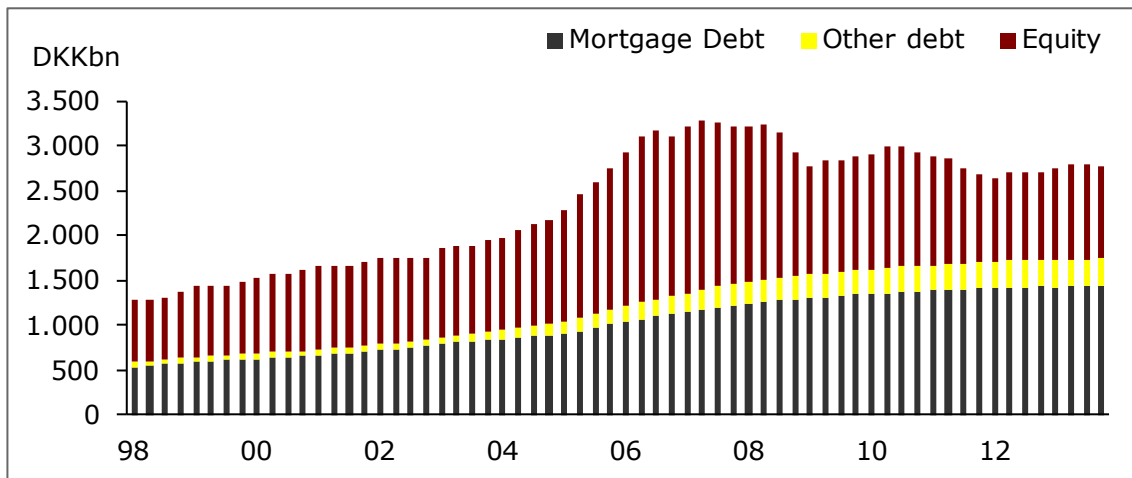
## House Price Trends

- House prices are now stable
- House prices are down 21% for detached housing from the peak mid 2007
- Expectations are for house prices to continue the current stabilization
- Number of houses sold is still low



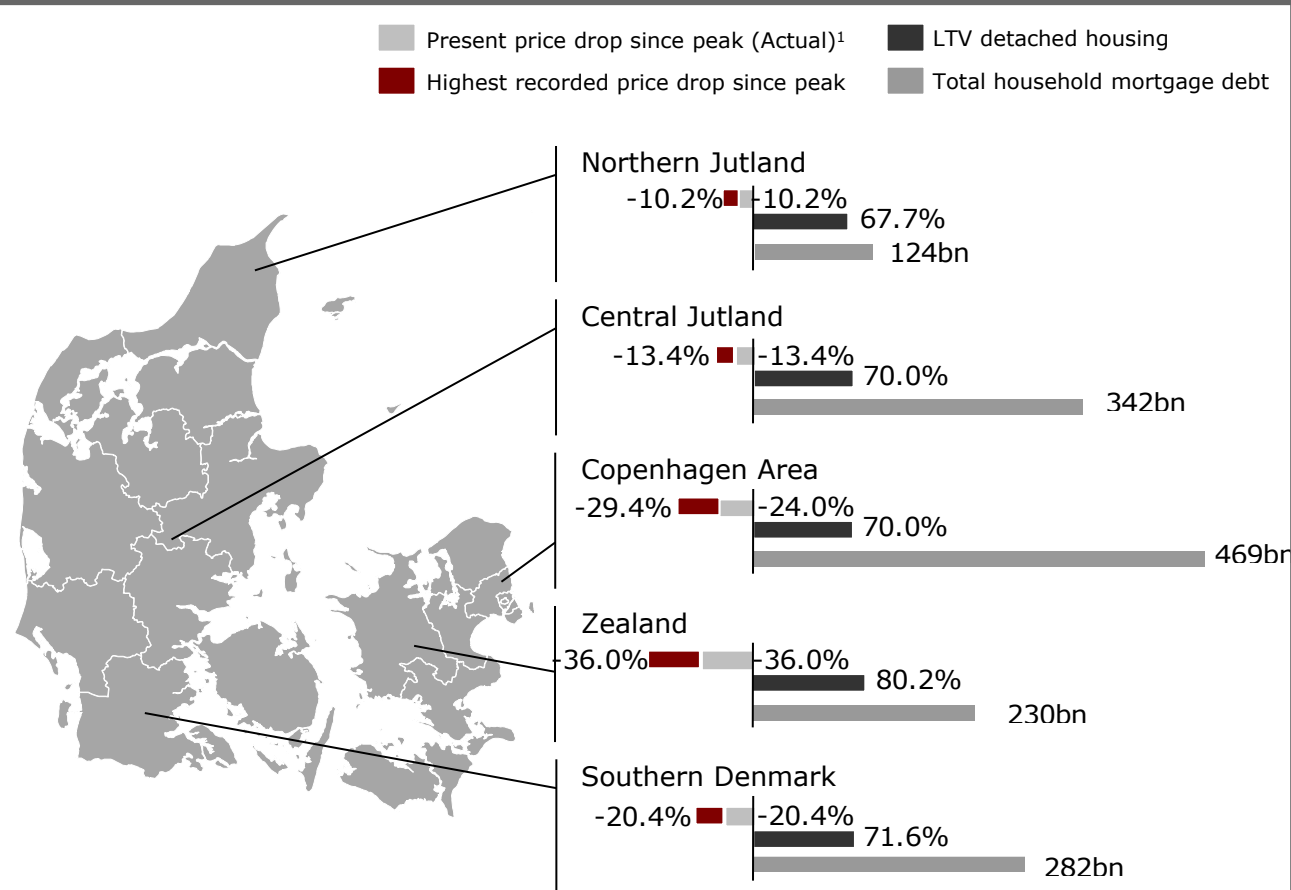
## Homeowners Equity

- Homeowners' equity was 1.022bn end 2013Q4 – down by 866bn since the peak in 2006Q3
- In the same period total lending increased by 446bn
- Hence, 52% of the drop in homeowners' equity can be explained by additional lending. 48% is due to house price deflation



# 1 Geographical Dispersion

## Private lending in Denmark in total



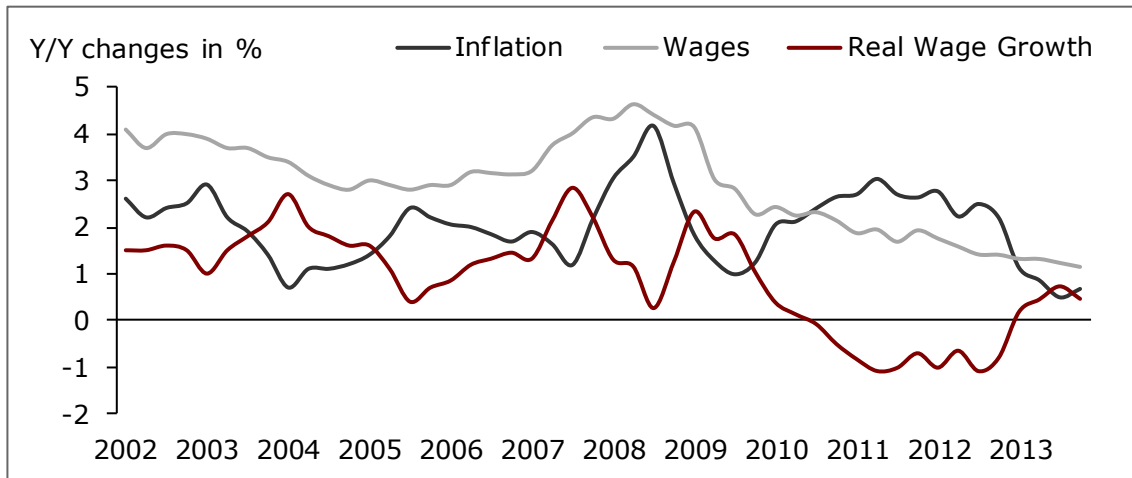
- House prices are now on a 2005 level
- The Copenhagen area was the first to suffer from house price deflation during the crisis in 2008. Prices are now 24% down from the peak in mid 2006
- Total mortgage debt in the Copenhagen area is the highest in the country. However, LTV is only 70% and house prices are recovering
- Zealand has crossed an LTV of 80% and prices are not recovering yet

<sup>1</sup>. If present price drop is lower than the highest recorded price drop it means that prices are recovering

# 1 Unemployment and Real Wage Growth

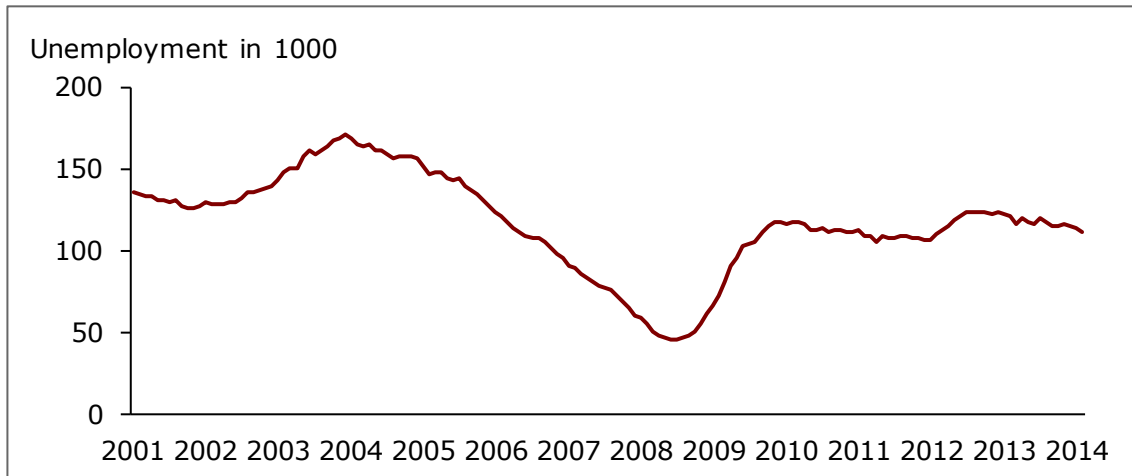
## Real Wage Growth

- Real wage growth in Q4 stood at 0.46%. 2013 was the first year with positive real wage growth after a period of 2.5 years with negative growth rates



## Unemployment

- Net unemployment stood at 114,680 end Q4 2013 up from a historical low of 45,000 in mid 2008
- This is equivalent to an unemployment (net) rate of 4.3%. Gross unemployment rate<sup>1</sup> is 5.6% end Q4 2013

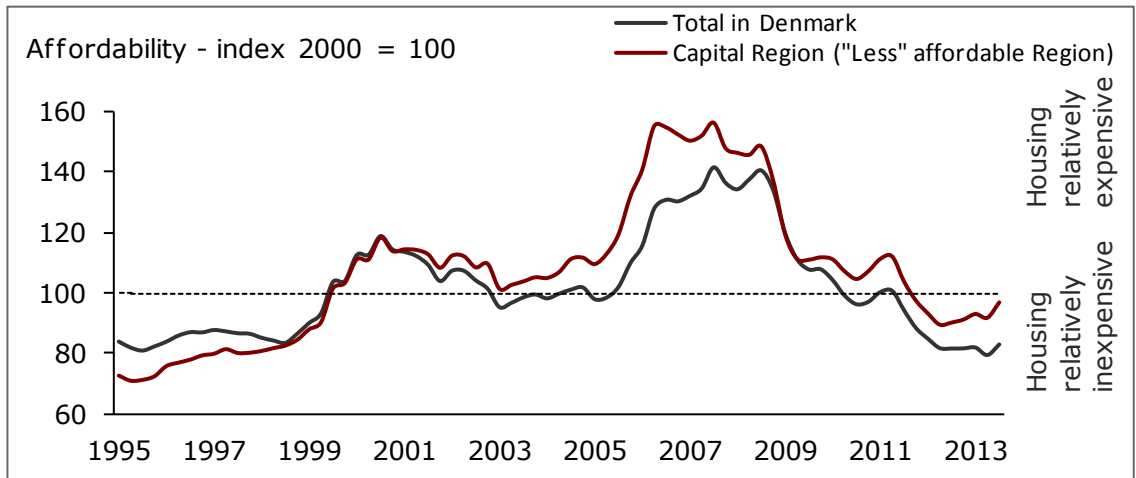


<sup>1</sup>. Gross unemployment rate defined as net unemployment plus persons in activation schemes

# 1 Homeowner Affordability and Foreclosures

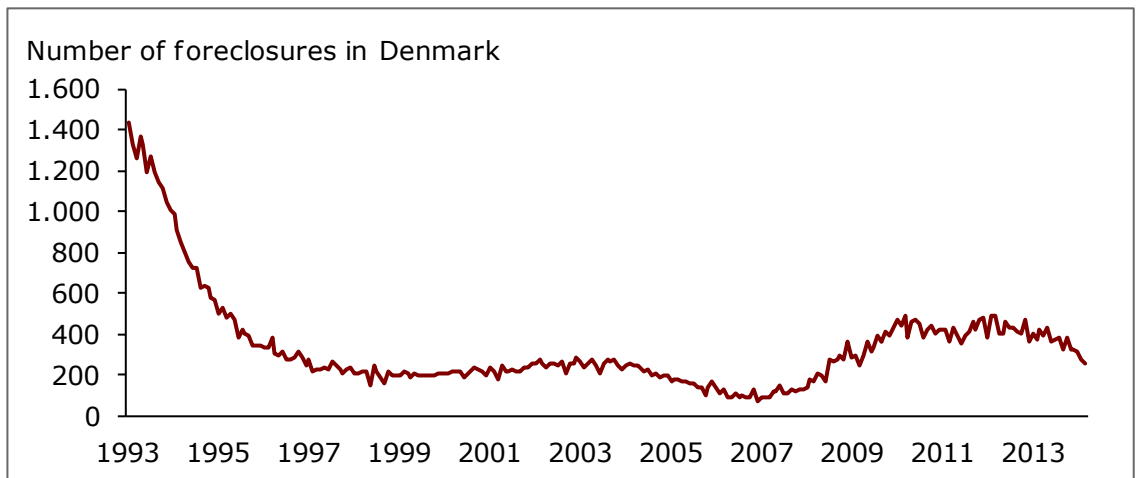
## Homeowner Affordability

- House price deflation and lower interest rates has made housing more affordable even in the Copenhagen area
- In Copenhagen the affordability index is getting very close to 100



## Foreclosures

- The number of foreclosed properties in Denmark in March 2014 was 254
- The duration of a foreclosure is approx. 6 months from missed payments to completion



# 1 Political measures and outlook

| Denmark <span style="color: grey;">■</span> Euro Zone <span style="color: blue;">■</span> | 2013 |      | 2014 |      | 2015 |      |
|---|------|------|------|------|------|------|
| GDP   | 0.4  | -0.4 | 1.5  | 1.3  | 2.0  | 1.7  |
| Private Consumption   | 0.0  | -0.7 | 1.1  | 0.9  | 1.5  | 1.2  |
| Fixed investments   | 0.7  | -2.9 | 2.2  | 3.1  | 2.8  | 4.1  |
| Export  | 1.2  | 1.4  | 2.8  | 3.9  | 3.4  | 4.4  |
| Unemployment %  | 5.8  | 12.0 | 5.5  | 11.8 | 5.3  | 11.6 |

## Danish Economy Outlook

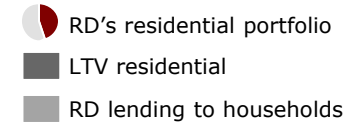
- The growth in the Danish economy is expected to increase to approx. 1.5 per cent in 2014
- European growth is expected to increase to 1.3 per cent in 2014
- Danish economy is highly dependent on exports which is expected to increase to 2.8 per cent in 2014
- Interest rates are a key element in the household economy. We still expect very low interest rates in the near future



# Key Collateral Indicators

Realkredit Danmark Specific Information

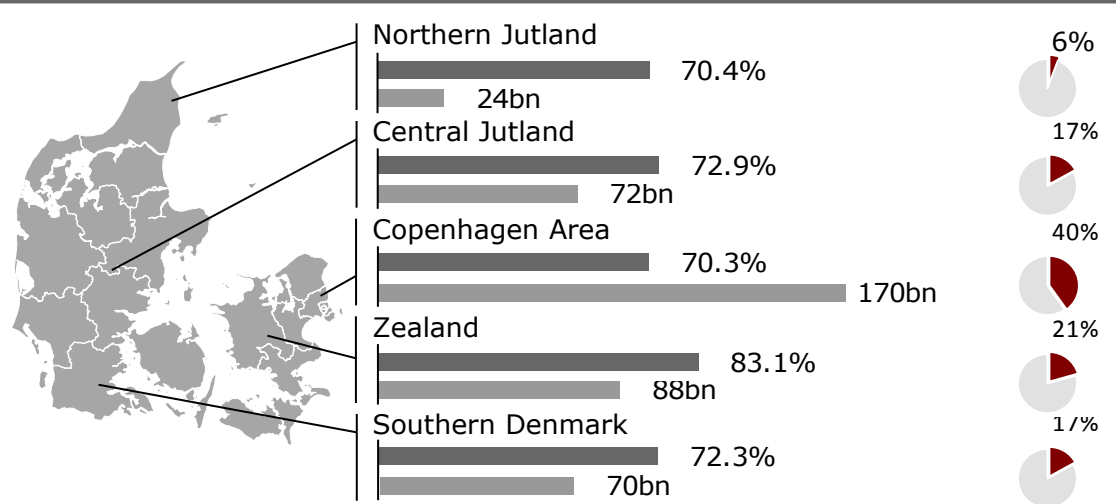
## 2 Dispersion and Loan to Value Ratios



### Dispersion of RD's residential portfolio

- RD's loan portfolio is concentrated in the Copenhagen area and on Zealand where prices have been reduced the most
- Homeowner equity remains highest in the Copenhagen area which also is the region with the smallest LTV
- Although the affordability ratio in the capital region is rising it is still below index 100
- Household mortgage debt in Q4 2013 was recorded at similar levels as Q3 2013

### Geographical Dispersion in Realkredit Danmark



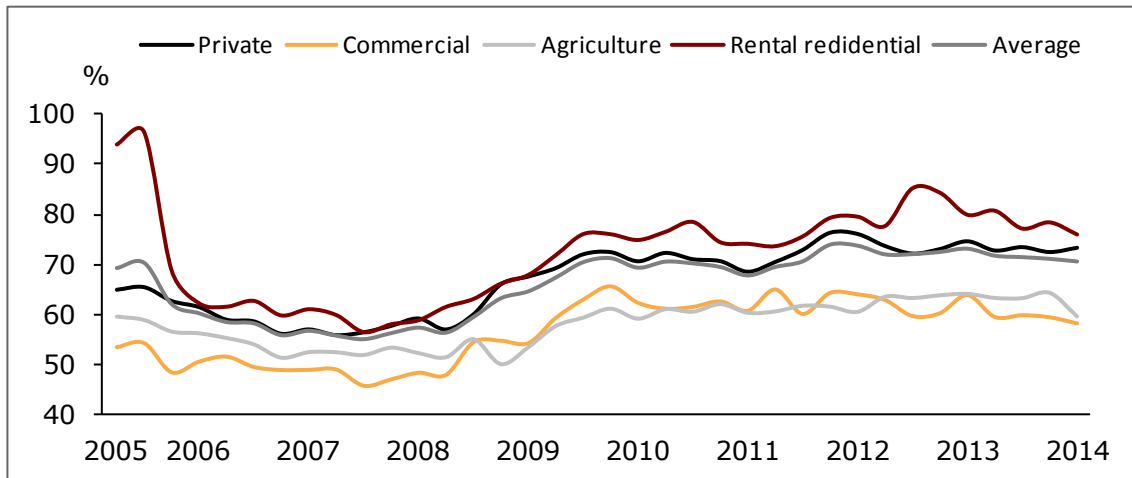
### Loan To Value Ratios

- Covered bonds are secured by a first claim on the mortgage collateral and the reserves of the issuer
- LTV ratios of the mortgage collateral are maximised by legislation at 80% in residential segments and 60% in commercial segments (70% if the outmost 10% are secured by additional collateral). Lending beyond these limits is prohibited
- LTV ratios are monitored on an ongoing basis based on current market values of the property and current prepayment value of the mortgages
- 34% of mortgage collateral securing covered bonds issued by Realkredit Danmark has a current LTV ratio of 20% or less. More than 62% has a current loan to value ratio lower than 40%
- Foreclosure costs are typically less than 15% of the outstanding loan balance

## 2 Loan To Value and Borrower Classifications

### Loan to Value

- Average loan to value ratios across market segments are 71% in Q1 2014 compared to 73% in Q1 2013
- LTV's for Commercial and Agriculture are based on few observations to confirm correct price levels



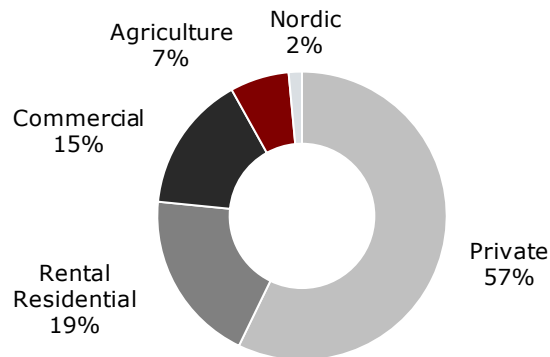
### Borrower Classifications

- Borrowers' financial strength is classified on a scale from 1 to 11, 1 being the highest score
- Approx. 8bn of total lending is secured by mortgages above the 80% LTV limit for which the borrowers' financial strength is classified 8-11 — equivalent to 1% of the portfolio

| DKKbn   | Rating Category (Scaled 1-11) |     |      |       |
|---------|-------------------------------|-----|------|-------|
|         | 1-3                           | 4-7 | 8-11 | Total |
| LTV     |                               |     |      |       |
| 0-20 %  | 48                            | 187 | 20   | 255   |
| 20-40 % | 33                            | 157 | 18   | 209   |
| 40-60 % | 21                            | 117 | 16   | 154   |
| 60-80 % | 10                            | 62  | 10   | 82    |
| > 80 %  | 8                             | 28  | 8    | 44    |
| Total   | 121                           | 550 | 72   | 743   |

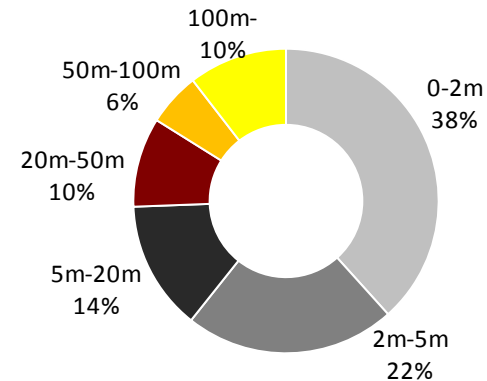
## 2 Collateral Breakdowns — Total portfolio

### Borrower Segmentation



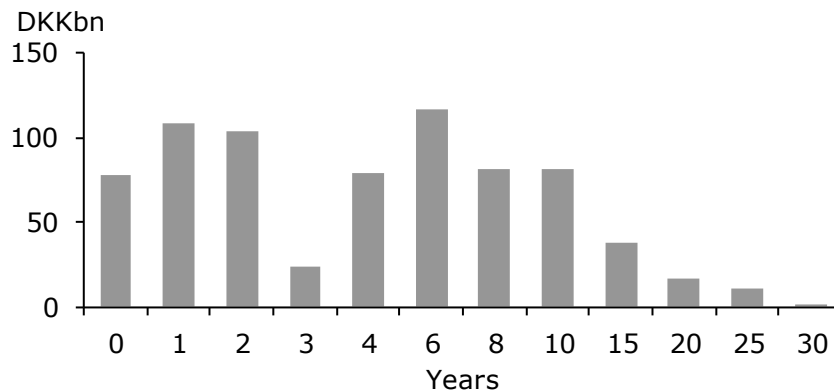
Note: Total lending distributed on segments

### Outstanding Loan Balance



Note: Total lending distributed on outstanding loan balances

### Portfolio Seasoning



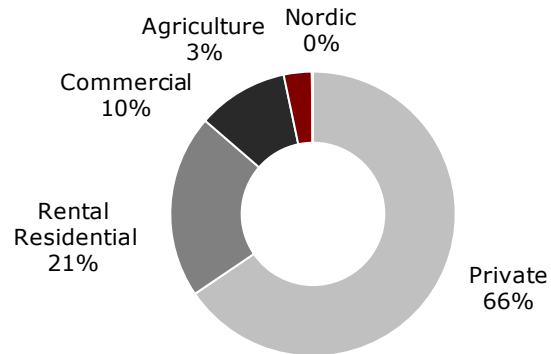
### Outstanding Debt in DKKbn by LTV ratio

| Segment            | 0-20% | 20-40% | 40-60% | 60-80% | >80% | Total DKKbn |
|--------------------|-------|--------|--------|--------|------|-------------|
| Private            | 135   | 118    | 91     | 56     | 25   | 425         |
| Commercial         | 47    | 38     | 27     | 7      | 5    | 124         |
| Agriculture        | 19    | 16     | 10     | 4      | 1    | 49          |
| Rental Residential | 54    | 37     | 26     | 15     | 13   | 145         |
| Weighted dist.     | 34%   | 28%    | 21%    | 11%    | 6%   | 100%        |
| Total, DKKbn       | 255   | 209    | 154    | 82     | 44   | 743         |

Average LTV: 70.6%

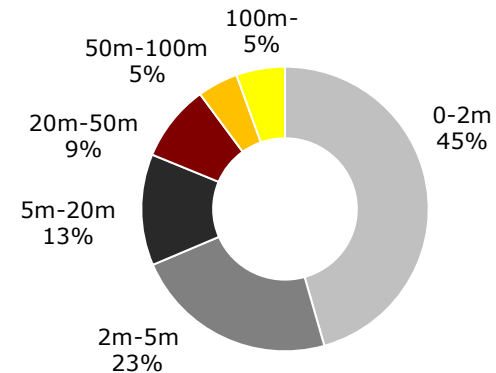
## 2 Collateral Breakdowns — Capital Centre S

### Borrower Segmentation



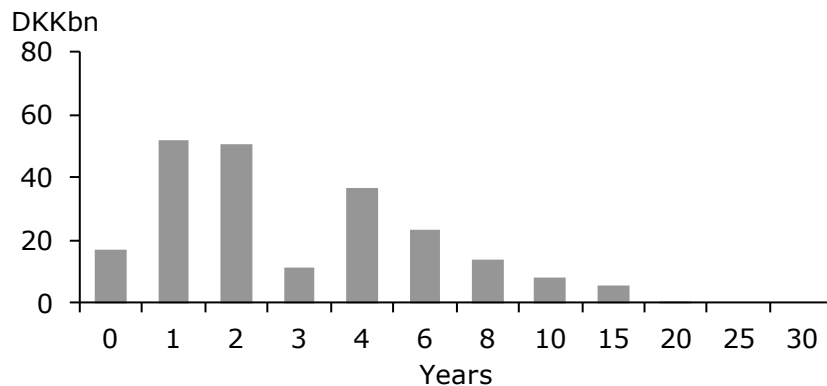
Note: Total lending distributed on segments

### Outstanding Loan Balance



Note: Total lending distributed on outstanding loan balances

### Portfolio Seasoning



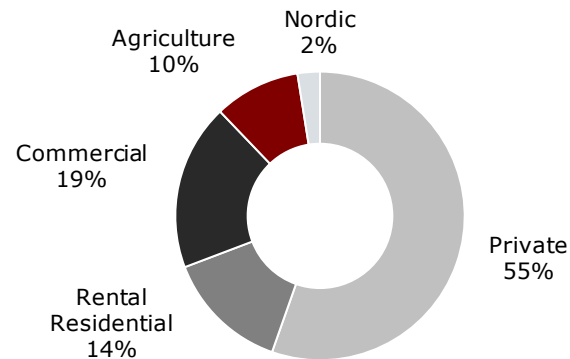
### Outstanding Debt in DKKbn by LTV ratio

| Segment            | 0-20% | 20-40% | 40-60% | 60-80% | >80% | Total DKKbn |
|--------------------|-------|--------|--------|--------|------|-------------|
| Private            | 43    | 40     | 32     | 20     | 8    | 143         |
| Commercial         | 7     | 7      | 5      | 2      | 1    | 23          |
| Agriculture        | 3     | 2      | 1      | 0      | 0    | 7           |
| Rental Residential | 19    | 12     | 7      | 4      | 3    | 46          |
| Weighted dist.     | 33%   | 28%    | 21%    | 12%    | 6%   | 100%        |
| Total, DKKbn       | 73    | 61     | 45     | 26     | 13   | 218         |

Average LTV: 69.4%

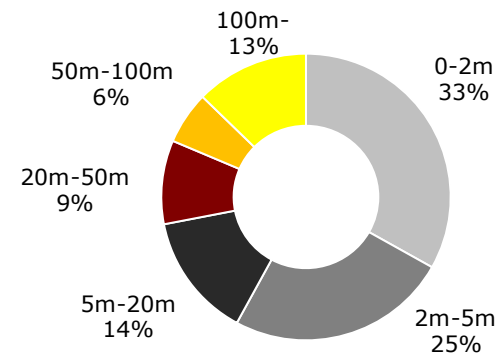
## 2 Collateral Breakdowns — Capital Centre T

### Borrower Segmentation



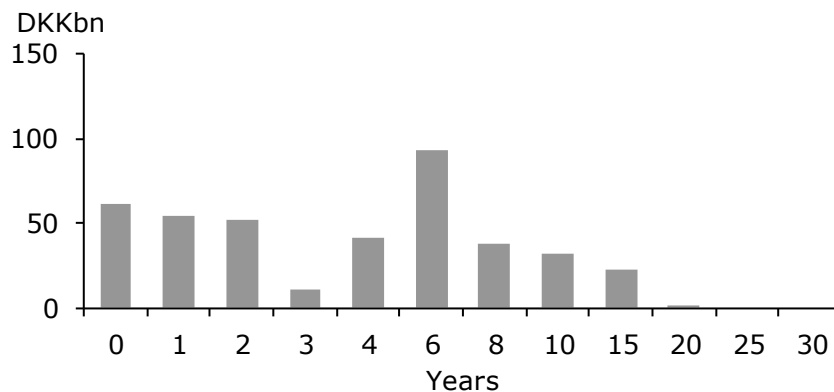
Note: Total lending distributed on segments

### Outstanding Loan Balance



Note: Total lending distributed on outstanding loan balances

### Portfolio Seasoning



### Outstanding Debt in DKKbn by LTV ratio

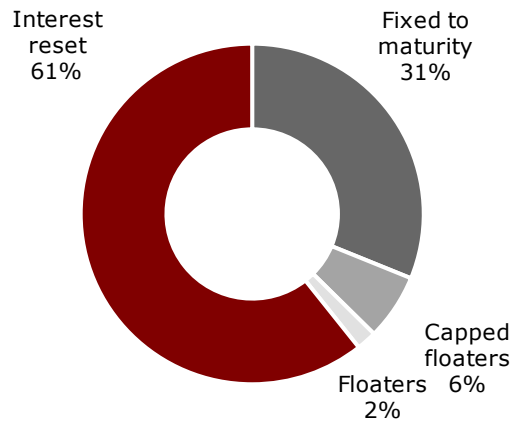
| Segment            | 0-20% | 20-40% | 40-60% | 60-80% | >80% | Total DKKbn |
|--------------------|-------|--------|--------|--------|------|-------------|
| Private            | 69    | 62     | 50     | 32     | 14   | 227         |
| Commercial         | 33    | 28     | 18     | 4      | 2    | 86          |
| Agriculture        | 15    | 13     | 8      | 3      | 1    | 39          |
| Rental Residential | 18    | 15     | 12     | 7      | 5    | 57          |
| Weighted dist.     | 33%   | 29%    | 22%    | 11%    | 5%   | 100%        |
| Total, DKKbn       | 135   | 117    | 89     | 46     | 22   | 409         |

Average LTV: 69.2%

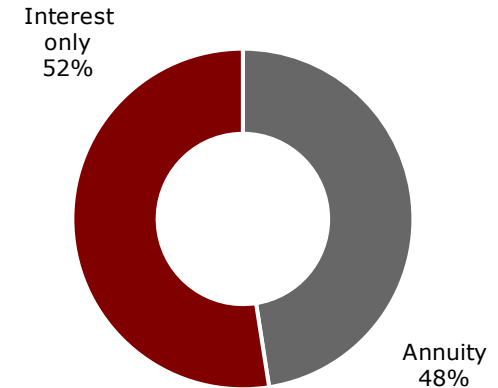
## 2 Borrower Exposure to Interest Rates

### Private Segment

- Homeowners must be able to service a 30-year fixed rate annuity loan for Realkredit Danmark to underwrite
- For the past decade borrowers have remortgaged from fixed rate into interest reset — now accounting for 61% of the loan book
- Expectations are for this trend to reverse since fixed rates are now 3.5% and FlexKort® (floater) is now offered as an alternative to interest reset loans
- 52% of the loans are interest only

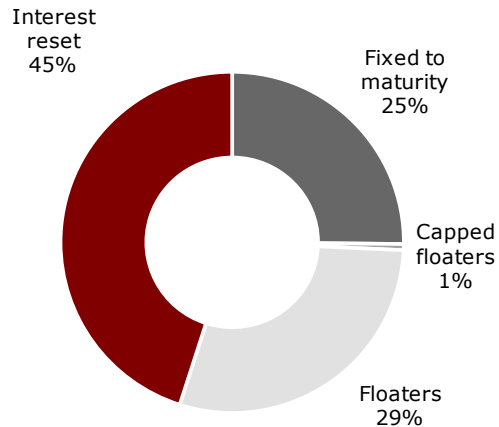


Note: Outstanding loan balances

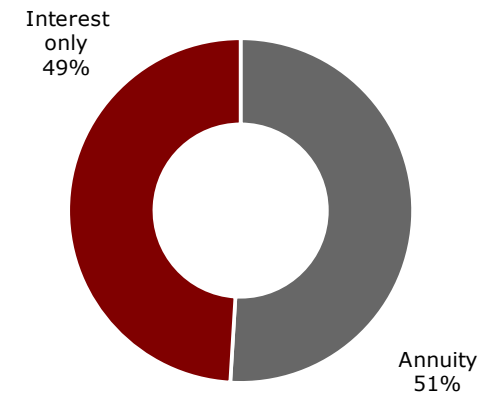


### Corporate Segments

- 25% of all lending in corporate segments is fixed rate to maturity
- More than 74% are either interest reset (typically, rates are reset every year or every third year) or floating rate (base rates are either 6M CIBOR, 3M EURIBOR or 6M CITA)
- Bullets and Interest only loans make up 49% of corporate lending



Note: Outstanding loan balances

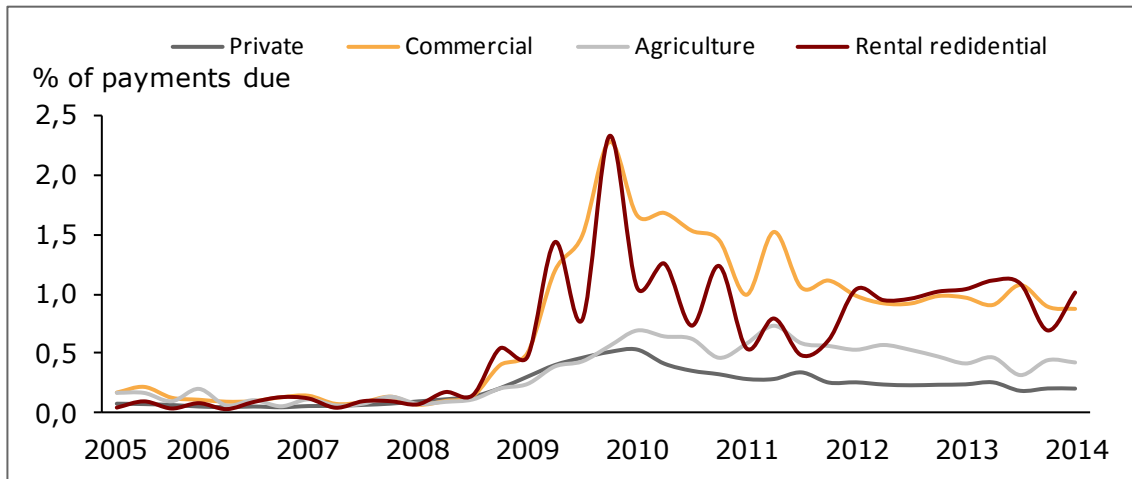


Note: Bullet loans are added in "Interest Only"

## 2 Arrears and Repossessions

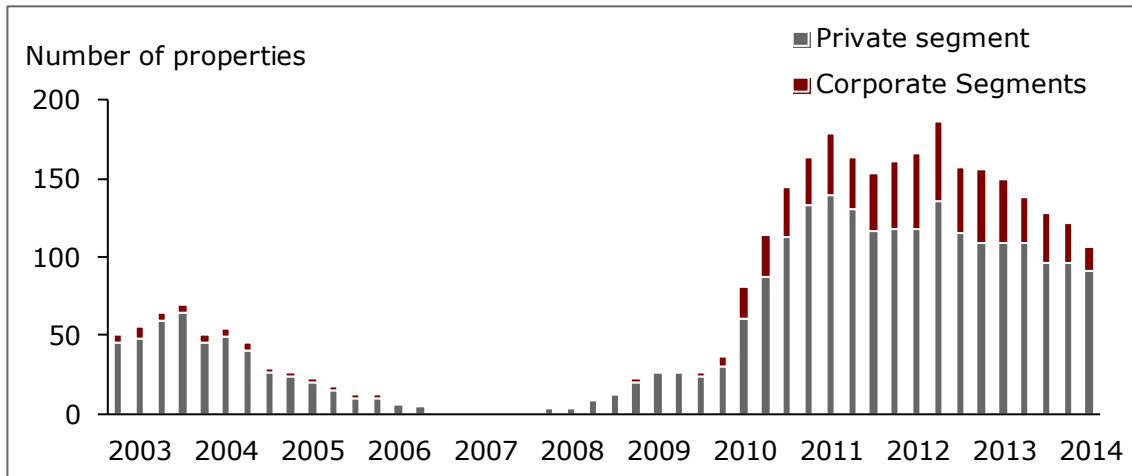
### Arrears (3 months)

- Total arrears stood at 0.54% end Q1 2014
- Arrears are rather volatile in the Rental residential segment. However, arrears are down considerably from Q4 2009
- Arrears in the Commercial segment is stabilising around 0.9%. Down from 2.3% in 2009, but up from normal levels of around 0.1% before 2009
- Arrears in the Private segments has been rather stable for the last years



### Repossessions

- The stock of repossessed properties stood at 107 end Q1 2014 — down 15 from Q4 2013
- This compares to a total stock of mortgage collateral at 500,023



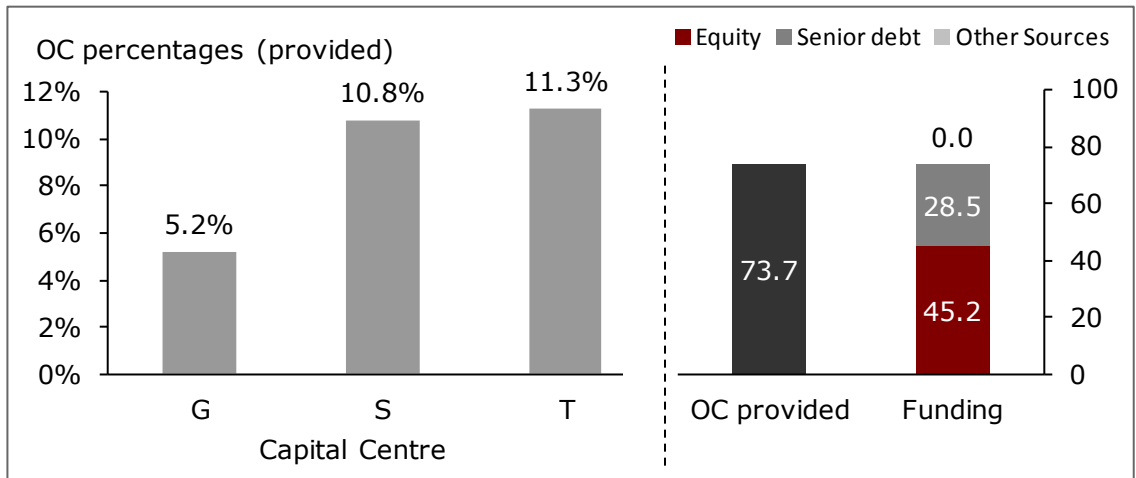


## 2 Over Collateralization and Capitalization

### Over Collateralisation

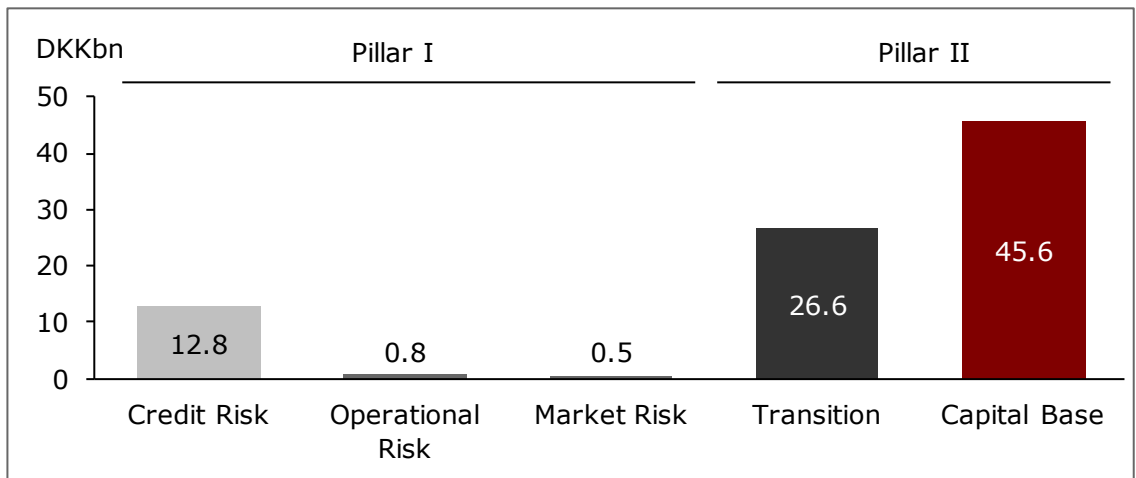
- Covered bonds issued by Realkredit Danmark are secured by mortgage collateral and reserves
- Reserves are invested in government exposures, covered bonds and bank exposures
- In case of bankruptcy Over Collateralisation will also be comprised by bondholders preferential claim

Note: Numbers per 1 April 2014



### Capitalisation

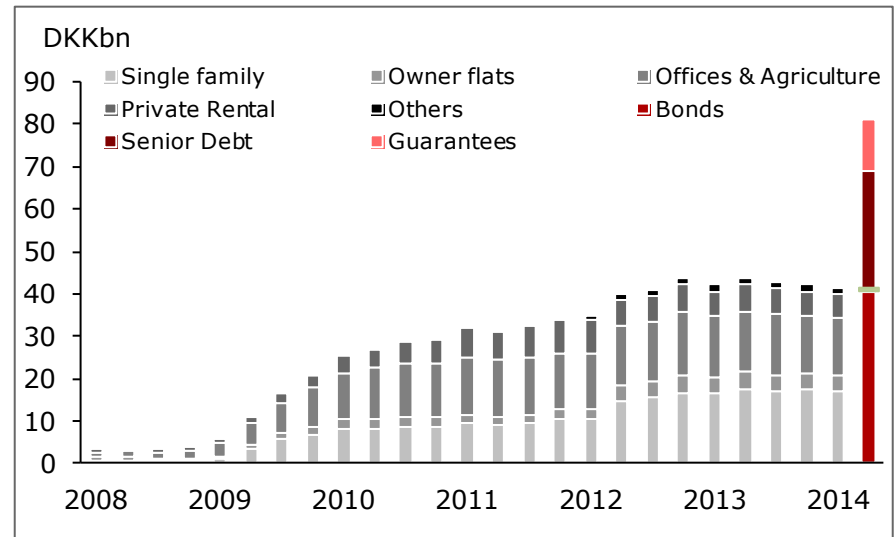
- The solvency ratio stood at 11.8% end Q1 2014 (CRD definition)
- Realkredit Danmark started issuing senior debt in Q1 2012 to strengthen the capital base



# Supplementary Collateral — Total in S and T

## Buffer in Capital Centres S and T

- End Q4 total OC provided was DKK 69.1bn in Capital Centres S and T of which 28.5bn was Senior debt
- Supplementary Collateral of DKK 41.4bn is required end Q1 2014 in Capital Centres S and T
- Loss Guarantees of DKK 12.0bn are utilised
- Buffer for further growth in need for supplementary Collateral in Capital Centres S and T is DKK 39.7bn
- If the OC is insufficient to comply with Supplementary Collateral requirements, RD can transfer OC from the General Capital Centre or write Loss Guaranties within the 15% limitation of issued bonds



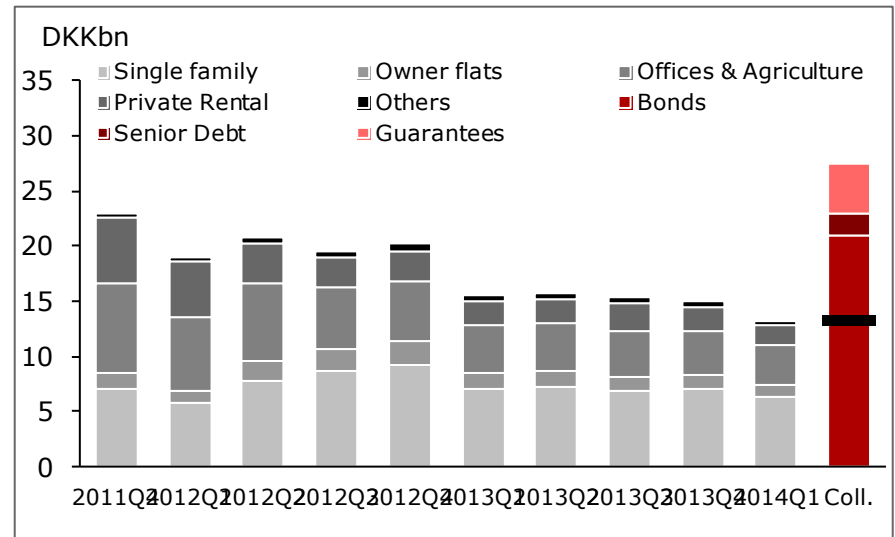
## Supplementary Collateral requirements

- If LTV limits are breached during the term of the loan the mortgage loan will only be eligible with the part that comply with the LTV limits. If eligible collateral is insufficient, Supplementary Collateral must be provided
- Increased need for Supplementary Collateral is due to
  - House price deflation
  - Properties selected for supervision
  - Refinancing and remortgaging of loans
  - Increased market value on bonds
- Loss Guaranties and eligible bonds can be used as Supplementary Collateral (bonds which also are used to comply with the solvency requirement) but no other asset types are eligible

# Supplementary Collateral — S

## Buffer in Capital Centre S

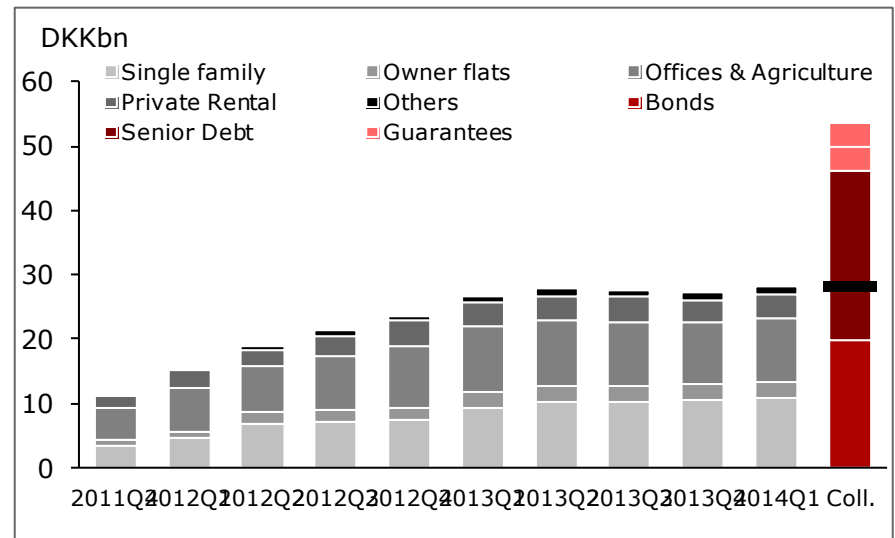
- End Q1 2014 total OC provided was DKK 22.9bn in Capital Centre S of which 2.0bn was Senior debt
- Supplementary Collateral of DKK 13.2bn is required end Q1 2014 in Capital Centre S
- Loss Guarantees of DKK 4.7bn are utilised
- Buffer for further growth in need for supplementary Collateral in Capital Centre S is DKK 14.3bn
- If the OC is insufficient to comply with Supplementary Collateral requirements, RD can transfer OC from the General Capital Centre or Capital Centre T or write Loss Guaranties within the 15% limitation of issued bonds



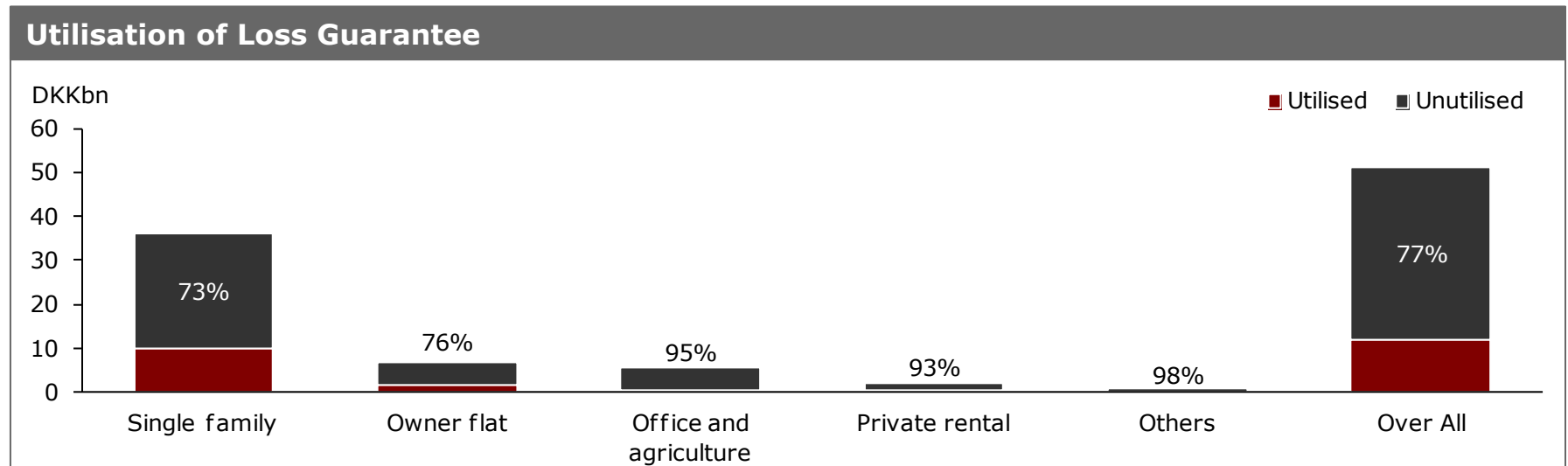
# Supplementary Collateral – T

## Buffer in Capital Centre T

- End Q1 2014 total OC provided was DKK 46.2bn in Capital Centre T of which 26.5bn was Senior debt
- Supplementary Collateral of DKK 28.2bn is required end Q1 2014 in Capital Centre T
- Loss Guarantees of DKK 7.3bn are utilised
- Buffer for further growth in need for supplementary Collateral in Capital Centre T is DKK 25.3bn
- If the OC is insufficient to comply with Supplementary Collateral requirements, RD can transfer OC from the General Capital Centre or Capital Centre S or write Loss Guaranties within the 15% limitation of issued bonds



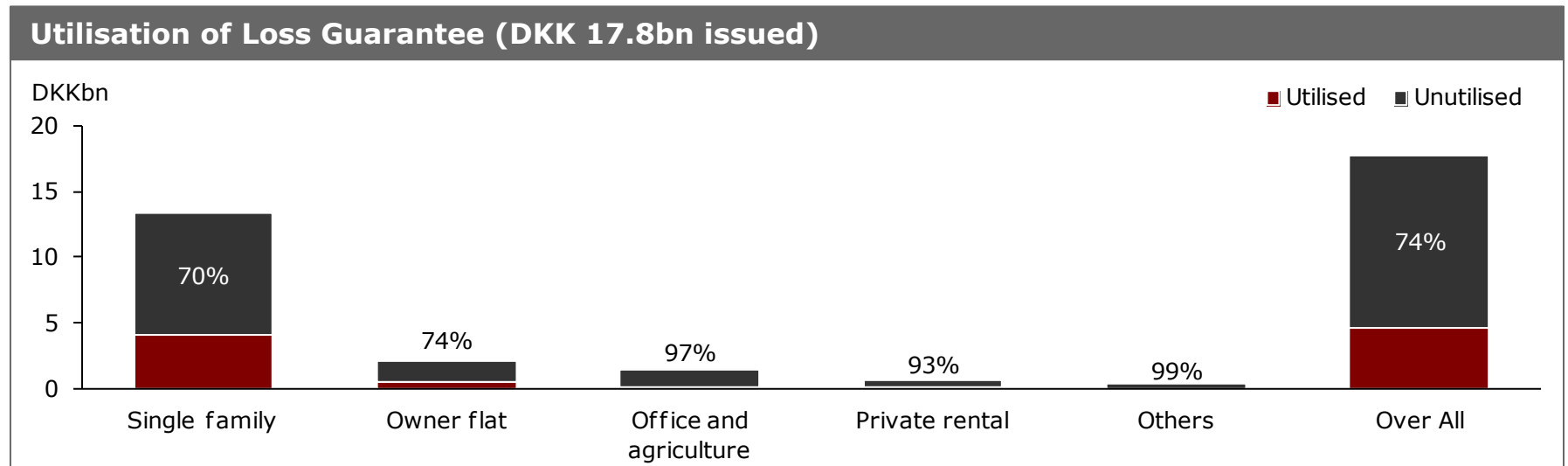
# Guarantees — Total



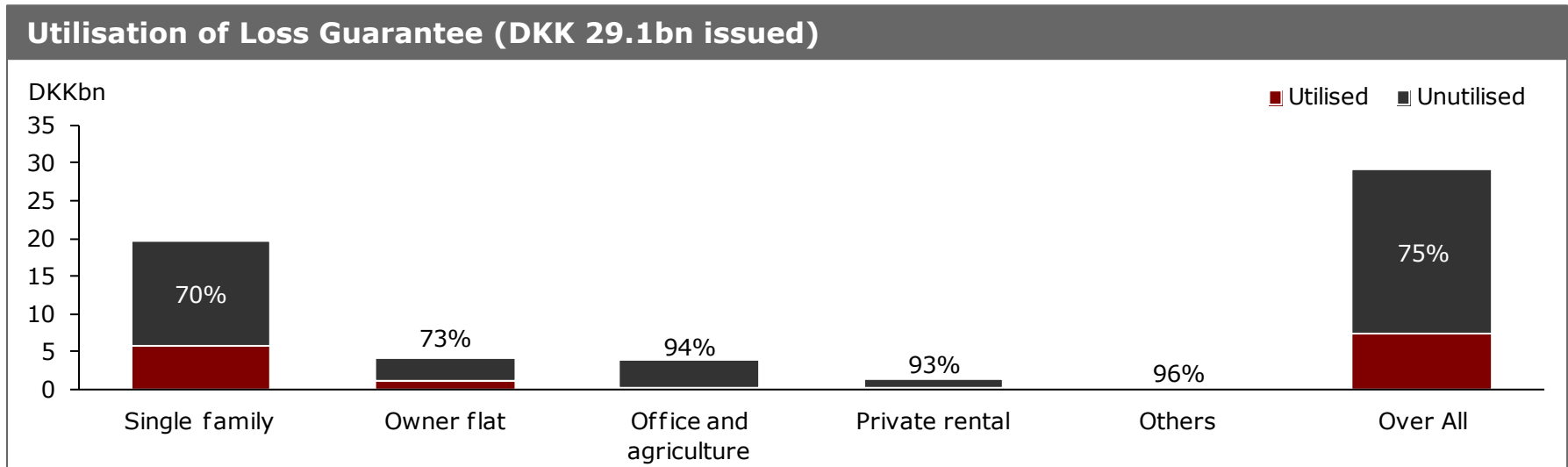
## Loss Guarantees issued by Danske Bank (DKK 51.2bn)

- RD loan disbursed through Danske Bank has a Loss Guarantee
- Loss Guarantees covers the outmost LTV limited to 20% of the maximum lending corresponding to LTV from 60–80% for Single Family Housing and 40–60% for Corporate and Holiday Housing
- Maturity of 8 years with an amortization equivalent to the covered loan
- Loss Guarantee covers losses obtained from forced sales including costs

# Guarantees — S



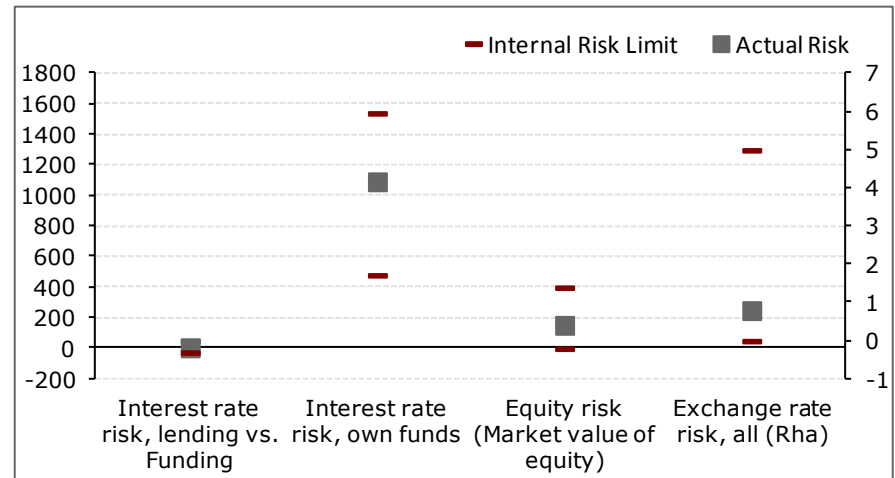
# Guarantees — T



## 2 Market Risk Exposure and Liquidity

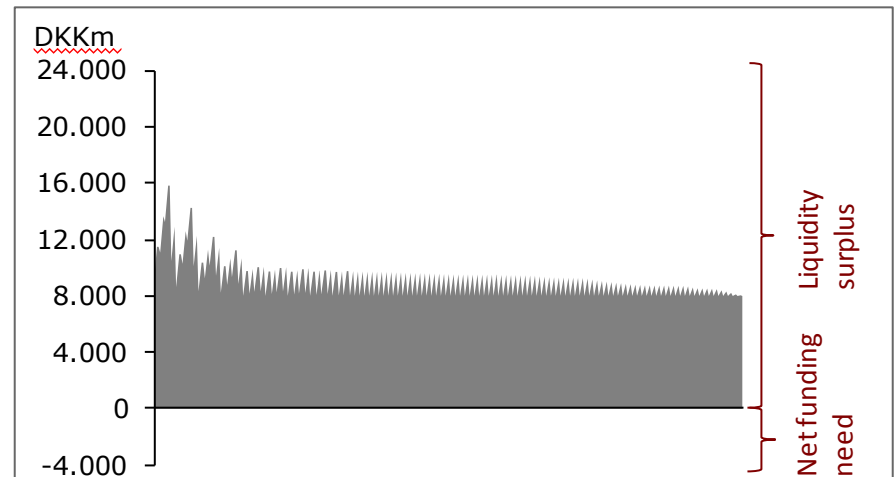
### Market Risk Exposures

- Realkredit Danmark operates subject to the specific balance principle
- In adherence with the principle Realkredit Danmark issues covered bonds on a daily basis to match loan origination and employs a pass through structure i.e. bond terms mirror loan terms
- Market risk exposures are, therefore, limited. End Q1 2014 interest rate risk on lending vs. funding stood at DKK 5.7m
- Derivatives are not employed for hedging imbalances on lending and funding



### Liquidity

- The pass through structure ensures a net inflow of liquidity from lending vs. Funding, i.e. Realkredit Danmark will not encounter a net funding need
- The liquidity inflow depicted in the chart does not include margin payments





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