Association of Danish Mortgage Banks' annual report 2014/15

Indhold

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Profile of the Association of Danish Mortgage Banks

The Association of Danish Mortgage Banks solely represents financial undertakings which are subject to Danish legislation and supervision and which use funding sources such as Danish covered bonds (”Særligt Dækkede Obligationer” – SDOs, ”Særligt Dækkede Realkredit Obligationer – SDROs, and ”Realkredit Obligationer” – ROs) to grant loans against mortgages on real estate.

As at 1 January 2015, the members of the Association are: BRFkredit a/s, DLR Kredit A/S, Nykredit Realkredit A/S and Totalkredit A/S.

The members of the Association represent nearly 57% of the total bond debt outstanding issued by Danish mortgage banks in Danish kroner (end-2014).

On behalf of our members, the Association strives to gain:

- Influence on the preparation and interpretation of legislation in Denmark and the EU to promote the interests and market position of the Danish mortgage industry, including as a minimum to ensure a level playing field for the mortgage system
- A strong voice in the public debate
- An overview of and insight into trends and changes in international legislation.

The Association works to maintain and develop a mortgage system which is characterised by a strict balance principle and transparency of prices and products, and which offers a flexible and market-based prepayment system.

It is our firm belief that the Danish mortgage model provides:

- Low and competitive prices of loans backed by mortgages on real estate
- Transparency of loan rates and prepayment terms
- Accessible financing for all people owning real estate
- Financial stability.

Chairman's statement

Winds of change are sweeping through Danish mortgage banking. We have coped well with the biggest crisis in recent times, but we are still struggling to adapt to the significant amounts of new regulation. More than ever, we are focused on creating value for our customers and for society, but we are also faced with growing demands and expectations from all sides. Adaptability has become a key concept in mortgage banking.

Especially the debate about mortgage banks' administration margins and the development in rural districts have attracted a good deal of criticism in the past year. Even though many of the driving mechanisms are largely beyond the sector's control, we are not oblivious to the fact that the debate is basically about whether you can have confidence in the mortgage system and the rest of the financial sector as a positive force in Danish society.

For we rely on confidence. Confidence that we put our customers first because they are our basis of existence. Confidence that we compete among ourselves for the benefit of consumers. Confidence that our practices and products are transparent. Confidence from investors who buy our bonds. And confidence from politicians that we are partners, not adversaries.

It will hardly come as a surprise when I say – Yes, you should have confidence in the Danish mortgage system. But the debate about prices and the willingness to extend credit shows that we need to become much better at explaining the motivation for our actions and, not least, why it is important to future-proof the Danish mortgage model for the benefit of customers and the Danish economy alike. That will be our task in the coming years.

Furthermore, a new and more nuanced dialogue about regulation is needed. A dialogue that is not about being for or against – or what could be perceived as whimpering or complaining – but rather a dialogue that is about striking the right balance between what we all want: security and growth at one and the same time.

We agree that there has been a general need to make the financial sector more resilient, even if the Danish mortgage system performed very well during the crisis. But now the time has come to let the numerous new rules set in so that we may evaluate their effect and take stock. Indeed, there seems to be a growing impression in Denmark that the regulatory process is coming to an end – at least for now.

Unfortunately, this does not seem to be the impression at the international level. Leverage ratio, minimum risk weights and capital floor are just a few of the international initiatives in play.

Moreover, despite increased focus on the consequences of the extensive regulation, nothing suggests that the EU's ambitions to harmonise the European financial sector are diminishing. The regulation is based on a conventional banking model, which is the most common in the EU and which does not accommodate the special Danish mortgage model.

This means that our model will remain under pressure in the coming years and that a concerted Danish effort is needed once again to influence and modify the international regulation. The aim is to preserve the Danish mortgage model that has offered affordable and stable property financing for more than two centuries.

Another point meriting special attention is the fact that an increasing amount of regulation fly under the political radar altogether as it is not discussed by the Council and the European Parliament. Instead it is dealt with by EU officials on the grounds that it is a matter of technicalities. However, these so-called technicalities are in fact of great importance to both the financial sector and the economy as such.

Regulation should generally be a parliamentary matter. We therefore hope that the politicians will take responsibility for striking a new balance between regulation of the sector and the desire for growth and prosperity.

We, the sector participants, will then assume the managerial responsibility which cannot be handled through regulation. For it is in the successful interaction between transparent regulation and strong managerial responsibility that we find the seed for a strong and secure financial sector of the future.

Cheap mortgage loans despite higher prices

Danish mortgage banks have raised their administration margins over the past few years. This should be seen as a direct consequence of the many new requirements for capital etc. imposed on the sector in the wake of the financial crisis. The requirements increase the resilience of the already very strong Danish mortgage model, but they also render it more expensive for mortgage banks to issue low-yield, AAA rated covered bonds for the benefit of homeowners, businesses and others. The rising administration margins cannot be seen in isolation from the low bond yields, and mortgage loans are still very cheap.

Rising administration margins have been a frequent topic in the public debate in the past year. The background is that the EU as well as Danish regulators require mortgage banks to hold more capital and implement initiatives that reduce the volumes of loans subject to refinancing, deferred amortisation or carrying a variable interest rate. The new requirements include:

- Capital conservation buffer: 2.5% of risk exposure amount (lending and other assets)
- Countercyclical capital buffer: 0-2.5% of risk exposure amount
- Systemic risk buffer (SIFI): 1-3% of risk exposure amount
- More capital of highest quality
- Debt buffer: 2% of total lending
- Supplementary collateral in case of falling property prices
- Payment to resolution fund
- Supervisory diamond for the mortgage sector

Additional initiatives are underway, including changed capital requirements for mortgage banks that apply the standardised approach for determination of capital requirements, a leverage ratio and new tougher capital floors (minimum capital requirements) for mortgage banks that apply the IRB approach for determination of capital requirements.

The new requirements imply that mortgage banks' capital needs have nearly doubled compared with before the crisis, see Chart 1, and that most of the capital must be in the form of Common Equity Tier 1 (CET1) capital, which is the most loss-absorbing and thus the most expensive type of capital. The additional capital must be procured in the capital markets or through the accumulation of earnings and profits. No matter how it is done, it will increase mortgage banks' cost of capital, while borrowers receive the entire gain to the extent that the improved capitalisation results in lower yields on the issued covered bonds. The increasing cost of capital is the primary reason why mortgage banks have had to raise their prices in recent years. Furthermore, mortgage banks have raised the prices of some product types to ensure that customer behaviour enables them to meet the requirements set out in the Supervisory Diamond for mortgage banks from 2018/2020. This applies especially to loans with high loan-to-value (LTV) ratios, loans subject to refinancing, deferred amortisation or carrying a variable interest rate, see Chart 2.

CONTINUED CONFIDENCE IN THE DANISH MORTGAGE SYSTEM

The increased capital requirements are intended to make financial undertakings more robust and resilient and thereby contribute to greater economic stability. The Association of Danish Mortgage Banks supports these goals.

Improved capitalisation of mortgage banks is also considered favourable by credit rating agencies, and together with sufficient earnings it forms a safeguard aimed at absorbing losses and securing the existing high ratings of Danish covered bonds. Most recently, rating agencies have responded to the new rules on the restructuring and resolution of mortgage banks and required mortgage banks to hold more capital to maintain their existing ratings.

Investors have always had great confidence in the secure Danish covered bonds. If we fail to meet the rating agencies' demand for improved capitalisation, it could have a negative effect on the bond ratings. That will entail higher bond yields and thereby higher prices for all borrowers. So higher administration margins are necessary if we are to be able to continue to offer the world's best and cheapest financing of residential and commercial properties, including agricultural properties. As long as Danish mortgage banks have their capital and ratings under control, they remain attractive to investors, and that makes for low mortgage rates. The low mortgage rates benefit customers, homeowners and businesses in full. Increased prices cannot be seen in isolation, but should be seen in conjunction with the mortgage rates resulting from the issuing of bonds.

HOW DOES THIS AFFECT HOMEOWNERS?

Whether an increase of the administration margin payable on a home loan is perceived as large or small depends on the finances of the individual homeowner. But numerous amounts have been mentioned in the debate about administration margin increases, some of them entirely out of step with reality.

The price (administration margin and price spread) of an average loan of DKK 1 million has increased by approximately DKK 100 per month for a fixed-rate repayment loan and approximately DKK 550 per month for an interest-only adjustable-rate mortgage (ARM) with 1-year interest rate reset (see Chart 2).

The administration margin increase depends on the type of loan. Especially interest-only loans and ARMs with 1-year interest rate reset have become more expensive, while the price of fixed-rate loans has not risen very much. The reason is the different risk profiles of the loans and the fact that mortgage banks use prices as one of the means to ensure a customer behaviour that is consistent with the restrictions set out in the Supervisory Diamond and elsewhere.

But despite the price increases, Danish mortgage finance is still cheap and compared with abroad, Danish homeowners, businesses and agriculture still enjoy markedly cheaper loans.

MORTGAGE LOANS CHEAPER IN DENMARK THAN ABROAD

In Sweden, the Swedish financial supervisory authority has computed an interest margin that is comparable with the Danish administration margin. As shown in Chart 3, the interest margin on Swedish home loans has risen more than the administration margin on Danish mortgage loans and is 50% higher.

In eurozone countries, citizens and businesses paid an average interest rate of 2.62% and 2.53%, respectively, in 2014 on new loans with interest periods of up to 1 year. By comparison, Danish homeowners and businesses paid 1.29% and 1.22% including administration margin on new mortgage loans with interest periods of up to 1 year.

An average variable-rate mortgage loan of a Danish homeowner is around DKK 1 million, and nearly DKK 14,000 a year should be added to the bill if homeowners had to pay the same interest rates as in the eurozone. Similarly, nearly DKK 60,000 should be added to the bill for businesses with a typical variable-rate loan of around DKK 5 million.

The total bill would be high if Danish homeowners and businesses had to pay the same interest rates as in the eurozone. For example, mortgage loans with short interest periods of Danish homeowners and businesses amount to some DKK 900bn, and it would result in additional costs of nearly DKK 12bn if Danish homeowners and businesses had to pay the same interest rates as in the eurozone.

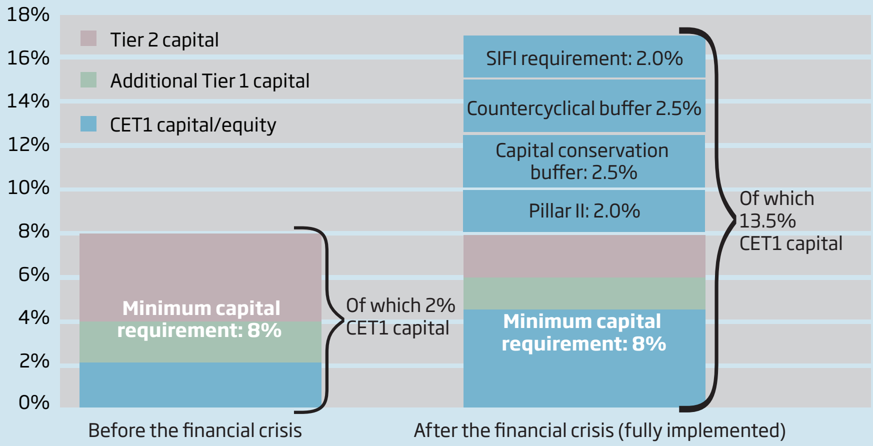
LOW EARNINGS FROM MORTGAGE LENDING

Mortgage banking generates relatively low earnings per DKK of loan. The return on equity (ROE) has averaged around 5% before tax for the last ten years. By comparison, Danish C20 companies generated an average annual ROE of 22% in the same period.

Even though the Danish mortgage system is a very secure business model, 5% ROE is at the low end of the scale and this may potentially affect the ratings of Danish covered bonds. It may affect the yield that investors demand for investing in the bonds issued by mortgage banks and thereby the mortgage rate payable by borrowers.

Chart 1:

Minimum capital and capital buffers



Source: Association of Danish Mortgage Banks

Capital must constitute at least 8% of a mortgage bank's total risk exposure amount (the risk exposure amount is the mortgage bank's lending and other assets weighted according to riskiness). Add to this an internal capital adequacy requirement (Pillar II requirement), estimated at around 2% of the total risk exposure amount.

Furthermore, there are new requirements of regulatory capital buffers calculated on the basis of the total risk exposure amount. A capital conservation buffer of 2.5% applicable at any time. A countercyclical capital buffer aimed at strengthening the resilience to economic trends. The buffer will vary between 0% and 2.5% of risk-weighted assets depending on the economic climate. The buffer is currently set at 0%. A systemic risk buffer the size of which depends on the systemic importance of the institution. The buffer is currently up to 2% for mortgage banks. The buffer requirements will be phased in gradually towards 2019.

Chart 2:

Administration margins and price spreads on different loan types – owner-occupied dwellings

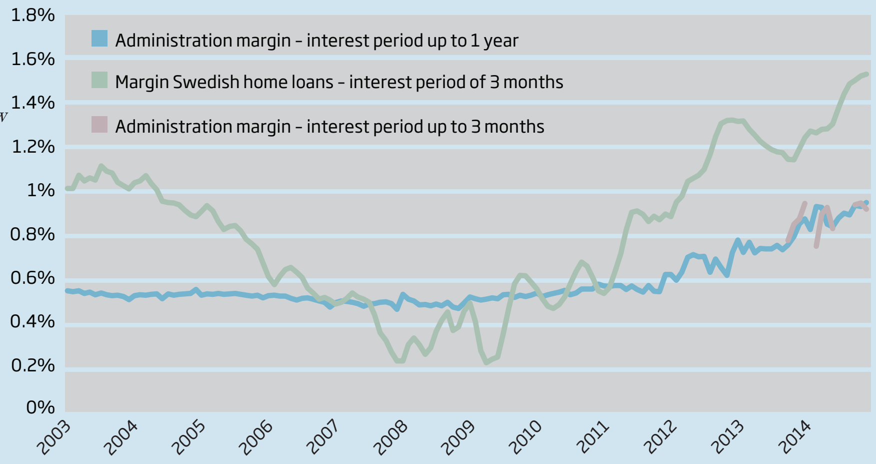
The source of administration margins for 2007 is Danmarks Nationalbank (average of new loans)

The source of administration margins and price spreads on refinancing for 2015 is averages of the institutions' price sheets for March 2015

Loan type	Administration margin and price spread on refinancing after tax, DKK		Difference after tax, DKK	
Loan of DKK 1 million	2007	2015	Annually	Monthly
Fixed-rate repayment	3,205	4,499	1,294	108
Fixed-rate interest-only	3,205	6,479	3,275	273
Repayment, 3Y/5Y interest reset	3,205	7,139	3,935	328
Interest-only, 3Y/5Y interest reset	3,205	9,120	5,915	493
Repayment, 1Y/2Y interest reset	3,205	7,843	4,639	387
Interest-only, 1Y-2Y interest reset	3,205	9,824	6,619	552

Chart 3:

Margins on new Swedish home loans to households and administration margins on new mortgage loans to households in Denmark, %



Source: Danmarks Nationalbank, Swedish FSA

Capital requirements for mortgage banks

1ST WAVE - ADOPTED MEASURES

The requirement for Common Equity Tier 1 (CET1) capital of mortgage banks increases from 4% in 2014 to 13.5% in 2019.

The increased requirement results from new legislation on capital buffers. These buffers are not optional, they are regulatory buffers. The buffers will be up to 7% for mortgage banks when fully phased in. Furthermore, the internal capital adequacy requirement for mortgage banks – the so-called Pillar II requirement – has increased since the financial crisis and is estimated at around DKK 2% of risk-weighted assets.

Add to this the requirement of supplementary collateral, which means that Danish mortgage banks have set aside over DKK 130bn of top-up collateral due to the lower property prices compared with before the crisis.
Lastly, in March 2015 the Danish parliament adopted a debt buffer requirement for mortgage banks in addition to the capital requirements and capital buffers. The debt buffer has been set at 2% of a mortgage bank's total lending, corresponding to just over DKK 50bn for the sector as a whole.

All in all, mortgage banks are facing increasing capital requirements due to the following:

- Markedly increased capital requirements laid down in new EU legislation
- Lower property prices than before the crisis that require supplementary collateral due to the requirement of continuous compliance with LTV limits
- Increased loan losses and impairments compared with the pre-crisis period.

2ND WAVE - MEASURES UNDER IMPLEMENTATION

The EU rules include a requirement for banks and mortgage lenders to disclose their leverage ratios. A leverage ratio is a non-risk-weighted measure of the ratio between an institution's capital and balance sheet total, whereas the capital requirements already implemented are risk-based. Furthermore, the introduction of a binding leverage ratio requirement is being considered at both the Danish and European levels. The Basel Committee has proposed a requirement of 3% for the total portfolio. Depending on the level, the introduction of such a requirement may imply yet another increase in the capital requirements for mortgage banks.

3RD WAVE - NEW MEASURES

New rules regarding the capital requirements for financial institutions are being discussed by European supervisory authorities and at international level. The Basel Committee is considering the introduction of a new permanent floor (backstop) to the capital to be held by institutions using IRB approaches to determine capital requirements. If this subsequently leads to EU rules, mortgage banks, which only offer loans against mortgages on real estate and thus incur low risk on their lending, could be faced with increased capital requirements. Lastly, there are changed capital requirements for institutions using the standardised approach to determine capital requirements.

Banking union and Danish mortgage lending

Denmark has not yet decided whether to join the banking union, but a report prepared by an inter-ministerial working group concludes that, overall, it will be an advantage for Denmark to participate. However, the report also emphasises that a solution must be found which can preserve the Danish mortgage model in the banking union.

The European banking union was established for the purpose of European banks, which are structured in an entirely different way than the Danish mortgage system. Therefore, there is a risk that Danish mortgage banks will be treated unfavourably in the harmonisation of rules and practices which is one of the aims of the banking union.

The banking union is two-pronged: A single supervisory mechanism and a single resolution mechanism including a common deposit guarantee scheme. The deposit guarantee scheme for the banks of the participating countries implies that on the one hand, the countries are liable for the debt of each other's banks and on the other hand, the participating countries – including potentially Denmark – are covered by "insurance", should their banks fall into trouble.

The other element – a single supervisory mechanism – became a reality in November 2014. The European Central Bank (ECB) has the overall responsibility for the supervision of all eurozone banks and carries out the direct supervision of the 130 largest financial undertakings. If Denmark opts to join the banking union, the ECB will gain influence over the Danish mortgage model through its supervision of mortgage banks.

In most EU member states, home loans are typically granted under a bank finance model. In Denmark, home loans are typically mortgage loans issued by specialised banks – mortgage banks – according to special rules. In its supervisory role, the ECB must adhere to a single rule book mindset – ie identical rules for all financial undertakings. And a decision made by the ECB in respect of an undertaking in another European country will also apply to Danish financial undertakings because of the principle of equality. It is important that the Danish mortgage model is not put at a disadvantage in the implementation of this principle. It is therefore a great challenge to ensure that the ECB understands the Danish mortgage model – and its significance to Denmark and the Danish economy.

In its report from April 2015, the government examined the pros and cons of potential Danish participation in the banking union.

The report points to a number of uncertainties and unclear issues in the relationship between the banking union and the Danish mortgage model. In respect of the supervisory mechanism, for example, the ECB's supervision could create uncertainty about the interpretation of EU rules. It also applies to the relationship between national adjustments of EU rules and the ECB's assessment thereof. In addition, there is some uncertainty about how the covered bonds that fund Danish mortgage loans will be treated in an international context. Also, the view of the European resolution mechanism on the resolution element needs to be clarified. The reason is that, to a large extent, the Danish mortgage model will not be subject to the European resolution model.

Danish participation in the banking union should be subject to a guarantee that Denmark can preserve the world's best and cheapest property finance system for the benefit of homeowners and businesses. Before deciding to join the banking union, the Danish government should be given reassurances that the Danish mortgage model is safe.

The mortgage sector is not shutting down rural districts

In recent years, mortgage banks' credit policies have been at the centre of the political debate about the challenges faced by rural districts in Denmark. But the mortgage banks are not the problem. Structural and political factors are at the root of the challenges. Thus, it is wrong to claim that "the mortgage sector is shutting down rural districts". The mortgage banks provide loans in all parts of Denmark, but some rural districts are challenged by various fundamental factors. Since World War II, these rural districts have experienced losses of private and public-sector jobs and depopulation. One of several reasons is that public-sector reforms have contributed to shutting down public-sector jobs and centralising hospitals, educational institutions, etc in the large cities of Denmark.

MORTGAGE LENDING MUST BE SECURE – ALSO IN FUTURE

In order to obtain a mortgage loan, the customer undergoes a credit assessment and the property is valued. Banks typically have the main responsibility for the credit assessment, while the property valuation is conducted by a mortgage bank. Both elements are very important. It is certainly in the customer's best interest that their personal finances are sufficient to make the mortgage payments. At the same time, the mortgage bank needs to know that the loan is secured if unforeseen events occur, such as long-term unemployment, critical illness or divorce, and the property has to be sold.

Mortgage loans are highly attractive as they offer very cheap home financing, and in Denmark a large number of people can afford to buy their own homes. Mortgage loans are cheap because they are based on a very high degree of security and low losses, and the pension savings of many Danes are invested in, for example, covered bonds. The losses incurred on mortgage lending have to be very small, and no one is automatically entitled to a mortgage loan.

Mortgaging of properties in rural districts involves an increased risk, and mortgage banks record markedly higher loss ratios for loans there compared with the large cities. It results in a direct cost, but also an indirect cost of capital, as the capital requirement for a loan depends on the arrears and losses on such properties. The cost of capital related to these loans is considerably higher than the expected losses.

If the development in a local community causes the mortgage bank to determine that a dwelling will be unable to maintain its market value, the mortgage bank will be forced to regard the dwelling as a "nondurable good" rather than an investment in an asset of stable value. In that case, the mortgage bank may, for instance, offer a loan below the maximum LTV limit or require that the loan must be repaid faster than the usual 30 years, or that it cannot include an interest-only option. Loan offers are customised. There is no lower limit to the loan amount. But in some cases, a loan can be so small that it becomes too expensive for the customer because of mortgage registration fees and other initial costs. In that case, a bank loan may be a better choice.

Even where the mortgage bank uses a flexible approach and offers the customer a loan, the home purchase may come to nothing. A good many purchase offers are made subject to full mortgage financing. If full mortgage financing is not offered, the buyer may find themselves in a situation where the credit assessment no longer holds true, or the buyer may opt to drop the purchase.

Mortgage banks' credit process is thorough – and the answer to a potential borrower is not always "yes". That is how it should be if we want to preserve the world's best mortgage system.

DENMARK IS CHANGING FOR SEVERAL REASONS

There are two main reasons why the Danish rural districts are struggling with the problems they have today. Firstly, Denmark has gone through a technological development that has changed the everyday lives of it citizens. Secondly, a number of political choices have been made about the structure of Danish society that have attracted people and jobs to urban areas.

According to a report by the Danish Building Research Institute (SBI) published in 2014, Denmark has since World War II undergone a period of urbanisation driven by the development in society. Agriculture and manufacturing have been replaced by service and knowledge-based industries that are centered around towns and cities to achieve competitive advantages. Many people have taken advantage of the various offers available in urban areas. The local businesses in small communities have felt the consequences of this, seeing customers being attracted to the large shopping centres.

Rural-urban migration has been going on for a long time and not only in Denmark. The same development is seen in many other countries, also in the other Nordic countries.
At the same time, many reforms have been implemented in the public sector, moving jobs away from rural areas, including a local authority reform, hospital reform, tax reform, police reform and court reform. Barracks, train stations and schools have been shut down. When schools close, families with children move away. If the train or bus no longer stops in the village, commuters and young people who can no longer get to their place of work or study move away. All these things act to shut down the small local communities.

Furthermore, it has been a clear political goal that young people should have an education so that they can take on future jobs. When educational institutions are mainly placed in the large cities, it is another factor that draws young people away from the rural districts. The significant net population growth recorded in Copenhagen these years is very much attributable to net migration of young people aged under 30.

POLITICAL RESOLVE IS REQUIRED TO CREATE A BALANCED DENMARK

The challenges of the rural districts originate from a fundamental change of our society over recent decades. If politicians want more people to settle down in rural areas, there have to be more jobs. Job creation need not only happen through relocation of public-sector jobs. We could also improve the conditions for entrepreneurs, SMEs and tourism.

No matter what, some rural districts today have many vacant houses that should be demolished to restore the balance between supply and demand. Politicians address the issue through the so-called demolition funds, but more funds are needed. According to the SBI in 2014, some 60,000 dwellings should be demolished and that would cost about DKK 5-6bn. This is considerably more than the demolition funds currently available.

COMMITTEE ON FINANCING OF RESIDENTIAL AND COMMERCIAL PROPERTIES IN RURAL DISTRICTS

At the request of the parliamentary committee for rural districts and the isles, Henrik Sass Larsen, the then Minister for Business and Growth, set up a committee in March 2015 on financing of residential and commercial properties in rural districts.

The committee is tasked with analysing and reporting on specific questions in relation to rules, conditions and practices for lending for private residential and commercial properties in the rural districts in Denmark. The committee will examine the rules governing mortgage banks' valuations, alternative sources of financing and experience from other countries.

If deemed relevant, the committee will submit concrete proposals to facilitate the financing of private residential and commercial properties in rural and peripheral areas. The proposals must not reduce the confidence in the Danish mortgage model and must not involve government financing or guarantees.

Professor Michael Møller of the Copenhagen Business School is chairman of the committee, and various stakeholders are represented on the committee, including the Association of Danish Mortgage Banks. The committee is expected to submit its report this autumn.

Better conditions for Danish agriculture

The agricultural sector is a significant factor in the Danish economy, so it is important to ensure the basis for its growth and development. Together with the Danish Agriculture & Food Council, the financial sector has focused on developing Danish agriculture.

The agriculture and food industries are vital to the Danish economy. The global market for foods and food technology is expanding rapidly and this opens the door to new business opportunities, especially in the emerging economies. The Danish food industry's long tradition of efficient production and sales in the international markets provides good opportunities for taking part in future growth.

But the basic framework has to be good, stable and competitive to deliver the required development in agriculture. The industry is extremely cyclical, and the Russian ban on EU goods has resulted in falling prices of, for instance, milk and pork. Large parts of the industry are doing well despite the difficult conditions – also in the international markets. Unfortunately, some farmers are in a difficult and vulnerable financial situation with unsustainable debt and liquidity levels. That makes it more difficult for this part of the industry to recover from the crisis.

It is in society's best interest to support the agricultural sector. It is a major industry that creates jobs and exports. To this end, the Danish Agriculture & Food Council, the Association of Danish Mortgage Banks, the Danish Mortgage Banks' Federation and the Danish Bankers Association agreed with the former government on a concerted effort to strengthen the development in the agricultural industry, including finding solutions to some of the industry's financial challenges.

The effort has the following focus areas:

- Reduction of the share of farms threatened by bankruptcy
- Focus on the high debt levels in the agricultural industry
- Easing of rules to make it more attractive to enter into reconstruction
- Focus on required investments, for example in barn systems
- Establishment of an investment fund, Dansk Landbrugs Kapital, with at least DKK 2 billion of capital. The fund is to contribute to a stronger financial framework for Danish agriculture and increasing investments in Danish agricultural businesses. The fund will operate on market terms.

The financial sector and the Danish Agriculture & Food Council will report annually on the work to reduce the number of farms with high debt and low liquidity levels.

New Act on restructuring and resolution of certain financial undertakings

It is essential to ensure the robustness of the mortgage sector as well as financial stability so that Danish homeowners and businesses continue to have access to stable financing of residential and commercial properties. Mortgage banks have a highly secure business model, and most recently the model's robustness has been reinforced with the debt buffer requirement. Also, it has been maintained that covered bonds cannot in any circumstances be bailed in.

In spring 2015 EU banking crisis management rules were implemented into Danish law with the Danish Act on restructuring and resolution of certain financial undertakings and by amendment of the existing financial legislation. With the new rules, the Danish FSA and Finansiel Stabilitet have been mandated to intervene earlier with institutions that are failing or likely to fail. The objective is to ensure the continuity of the institution's critical functions and avoid destabilising financial markets. Furthermore, the management of failing institutions should as far as possible take place without the use of government funds and thereby without costs to taxpayers.

NO ACCESS TO BAIL-IN OF COVERED BONDS

The key principle of the Danish resolution/bankruptcy model for mortgage banks is that the holders of the issued bonds must be protected to the greatest possible extent. To this end, claims from bondholders are satisfied in full by all future payments from the assets placed as security for the bonds, prior to the claims of all other creditors. Further, payments from borrowers to bondholders are not accelerated in case of bankruptcy. This enables an orderly resolution process with no risk of a loss of value through a forced sale of assets. It is achieved through slow repayment of the issued loans and bonds, potentially up to 30 years. In the more than 200-year history of the Danish mortgage system, no mortgage bank has ever been declared bankrupt and thus entered into resolution.

The implementation of the new EU rules introduced a number of tools for resolution of mortgage banks. The resolution tools include setting up of a bridge institution, separation of assets, and the sale of the business or shares of the institution under resolution. The new tools may only be applied provided that no creditor incurs greater losses than it would have incurred if the institution had been wound up in normal insolvency proceedings (the 'no investor worse-off' principle).

However, resolution of a mortgage bank can never take place by bail-in of Danish covered bonds (ROs, SDOs and SDROs). This follows from the fact that in the EU rules Danish mortgage banks are exempt from the requirement of bail-inable debt.

DEBT BUFFER INCREASES RESILIENCE

The new tools for resolution of mortgage banks have been supplemented with a debt buffer requirement. The debt buffer is a supplementary national requirement alongside the capital requirements and capital buffers. The buffer has been set at 2% of a mortgage bank's total lending and will be phased in towards 2020.

The debt buffer is to be applied where a mortgage bank becomes distressed and where the capital base is gone and can turn positive by means of the buffer. The buffer will contribute to greater certainty that the mortgage bank can carry on the systemically most important functions. This includes the ability to keep providing loans and thereby underpin financial stability. The buffer increases resilience and has positive effects from a credit rating perspective.

A debt buffer at 2% of total mortgage lending corresponds to just over DKK 50bn for the sector as a whole. The debt buffer will also include funds which the mortgage bank may use to provide supplementary collateral in case of falling property prices. The debt raised may thus to some extent replace the issuance of junior covered bonds, for example. But it is an added cost for the mortgage sector, as capital to fund a debt buffer will be more expensive than junior covered bonds. The reason is that the capital is bail-inable in case of crisis. The added cost will depend on the price of market funding, which varies over time according to the economic climate.

RESOLUTION FUNDS

With the new EU rules on banking crisis management, national, sector-financed resolution funds must be established that can be applied in connection with the handling of distressed financial institutions. As mortgage banks are exempt from requirements of bail-inable debt, they cannot be recapitalised through such a funding scheme. On the other hand, the resolution funds may support mortgage banks for example by way of guarantees or liquidity or on establishment of a bridge institution.

The national resolution funds must have funds corresponding to at least 1% of the amount of covered deposits of the institutions by 31 December 2024. The total contributions payable by mortgage banks to the resolution fund have not yet been determined. Mortgage banks have been granted a minor reduction given their limited possibility to use the resolution funds. Mortgage banks' direct contributions will amount to an estimated DKK 3.5bn.

New liquidity rule a potential threat to the Danish mortgage system

To prevent a recurrence of the financial crisis, the Basel Committee submitted a proposal for two new liquidity requirements for financial institutions in late 2009. One of them, the Liquidity Coverage Ratio (LCR), applies today in the EU. The other requirement, the Net Stable Funding Ratio (NSFR), is still being considered at EU level. It is absolutely crucial to the Danish mortgage system that the treatment of mortgage loans according to the current recommendations of the Committee in respect of the NSFR is adjusted before the rule becomes mandatory in the EU.

LCR

The LCR requirement, which requires a certain match between the cash flows of a financial institution over a short term (30 days), was determined finally in early 2015. The LCR enters into force on 1 October 2015 and will be phased in over the coming years. Danish systemically important financial institutions (SIFIs) must meet the requirement in full as of 1 October 2015. Under the LCR, only the largest covered bond series qualify as assets of the highest quality (Level 1 assets). As opposed to government bonds, which may make up the entire liquidity buffer, covered bonds may only represent up to 70%.

NSFR

The NSFR is to ensure a better match between financial institutions' lending and the funding thereof than was the case before and during the financial crisis.

The Basel Committee published their final NSFR recommendations in the autumn of 2014. At end-2016 the European Commission may opt to submit a proposal to the Council and the European Parliament for the introduction of the NSFR in the EU. This option is set out in the Capital Requirements Regulation (CRR).

The Association of Danish Mortgage Banks supports the efforts to ensure a better match between financial institutions' lending and the funding thereof. However, the final recommendations of the Basel Committee contain a number of undesirable features that should be eliminated before any implementation of the NSFR.

Generally, the recommendations place home loans funded by bonds of the SDO and RO types in a less advantageous position than home loans funded by other means, for example by deposits. The recommended rule is aimed at preventing inappropriate behaviour by universal banks. However, this provision will have a severe impact on specialised banks, such as the Danish mortgage banks, as their loans are based on issuance of SDOs and ROs. At the same time, seen from a stable funding perspective, the recommendations actually encourage banks to fund their lending with sources that are more unstable than SDOs and ROs.

It is essential that short-dated bonds with a statutory maturity extension feature be regarded as stable funding. We assume that the Danish authorities, in due time, will achieve recognition of the Danish solution for managing refinancing risk in relation to future EU rules. If not, we will be facing severe challenges as regards adjustable-rate mortgages with short interest rate reset periods. It would not be fair that borrowers would have to live with a poorer product range because the NSFR rules do not allow for the provisions of the Danish refinancing act.

In light of the existing errors and omissions in the final NSFR recommendations by the Basel Committee, it is positive that any implementation at EU level will be fine-tuned by the European Commission, the Council and the European Parliament. In that connection, the Association of Danish Mortgage Banks is also pleased that the report of the European Banking Authority (EBA) which will form the basis of any Commission proposals for NSFR rules must specifically include an assessment of how an NSFR requirement will impact matchfunded mortgage models such as the Danish mortgage model.

NSFR and funding mismatch

During the financial crisis, banks and mortgage lenders in many other countries experienced that it was suddenly difficult to raise capital to fund new and existing loans to their customers. The reason was that large parts of the financial sector had issued long-term loans to their customers, but had funded these loans with deposits and/or short-term funding from other banks. This funding mismatch created a need for ongoing refinancing. As uncertainty spread across the financial markets, it became difficult or impossible to refinance the short-term funding used by the institutions to fund their lending.

The purpose of the stable funding rule is to ensure an appropriate match between the maturity of the institutions' lending and deposits. More specifically, loans with a term-to-maturity over 1 year must be matched by stable funding. This means, for example, that a mortgage bank with a large proportion of long-term lending that is funded by short-term bonds will not comply with the NSFR requirement.

The NSFR has been introduced as a soft requirement with an observation period running until 2018 inclusive. The EBA must submit a report to the European Commission by 31 December 2015 based on the test reporting. The report must contain a recommendation on whether or not to introduce the NSFR as a hard requirement. If the Commission finds it appropriate, it will make a proposal to introduce the NSFR requirement. Such a proposal will then undergo a political process in the European Parliament and the Council. If adopted, the NSFR is expected to be phased in from 2018 at the earliest.

Covered bond legislation in the EU

The European Commission is currently examining the pros and cons of an EU law framework for covered bonds. The Association of Danish Mortgage Banks is positive towards this and is participating actively in examining the basis for such a framework. We find it imperative that an efficient mortgage market in Denmark is preserved. And we will argue that a mortgage model such as the Danish one should serve as inspiration at a European level, for instance how households and businesses alike can raise funding on capital market terms.

CAPITAL MARKETS UNION

In February 2015, the European Commission published a Green Paper entitled Building a Capital Markets Union. The purpose of a Capital Markets Union is to strengthen investment especially for SMEs and infrastructure projects. Other objectives include attracting more investment into the EU and making the financial system more stable by opening up to a wider range of funding sources, also outside the traditional banking system. The Green Paper is part of the Juncker Commission's objective of creating growth and jobs in the EU. In this respect, improved access to funding plays an important role.

The Green Paper also suggests that an integrated market for covered bonds can contribute by way of funding and new investment opportunities for some investors. However, the Commission does not propose any concrete initiatives, but will begin by conducting a public consultation to examine advantages and a possible structure of an EU covered bond framework, and will subsequently present a number of possible initiatives based on experience from efficient national models. The separate consultation on covered bonds is scheduled for autumn 2015.

DANISH MORTGAGE SYSTEM

We are generally positive towards the Commission's intention to examine the basis for introducing an EU law framework for covered bonds. In connection with the adoption of financial legislation in the EU after the financial crisis, there have been several examples that the unique Danish mortgage system has been put at a disadvantage because the legislation is based on a traditional banking model. The Commission's initiative may therefore offer a good opportunity for describing and codifying the elements that characterise an effective mortgage system such as the Danish one. We will therefore be proactive in examining the basis for a legal framework where emphasis is on preserving an efficient mortgage market in Denmark.

Supervisory Diamond makes a secure system even more secure

The Supervisory Diamond has five new indicators aimed at limiting the risk exposures of the individual mortgage banks. The indicators are well in line with the adjustments already being made by mortgage banks.

The Danish FSA has introduced a new set of indicators for mortgage banks. The five new indicators are entitled the "Supervisory Diamond for mortgage banks". They are symbolised by a diamond with five corners, each representing an indicator, see Chart 4. The purpose of the five indicators is to limit the risk exposures of the individual mortgage banks.

Critical voices could claim that if it is necessary to make rules, there must be something that is not working. But nothing could be more wrong. The Danish mortgage system has proved efficient for 200 years during both upturns and downturns in the Danish economy. The Danish central bank has even provided evidence that the mortgage system has made the Danish economy more stable during financial crises . But there is always a risk that something goes wrong in extreme situations, and the Supervisory Diamond is intended to pre-empt such risks. The indicators of the Supervisory Diamond are in line with the adjustments already being made by mortgage banks, including the spreading of refinancing risk.

The supervision of the Supervisory Diamond is based on quarterly reports from Danish mortgage banks to the Danish FSA. The reported values are measured against a set of fixed limit values for five selected indicators. If a limit value is breached, the Danish FSA will commence a dialogue with the institution concerned. Based on individual and concrete assessments, the Danish FSA may take action, for instance in the form of public risk information. The Supervisory Diamond consists of guidelines laid down by the Danish FSA, also known as "soft law". The soft guidelines leave more room for discretion and flexibility compared with "hard" or traditional law.

In the initial phase of implementation, mortgage banks will typically be outside the limits. The idea is for the institutions to gradually approach the targets of the Supervisory Diamond. Gradual implementation makes sense as mortgage loans have long loan terms. Therefore, mortgage banks cannot implement changes in the short term, and the indicators for interest-only loans and frequent refinancings will not take effect until 2020. The other indicators will apply from 2018.

The Supervisory Diamond contains the following indicators:

1) Interest-only loans
2) Limitation of lending with short-term funding
3) Borrower's interest rate risk
4) Lending growth
5) Large exposures

[1] Financial structures and the real effects of credit-supply shocks in Denmark 1922-2011, working paper 2012-78, Danmarks Nationalbank.

INTEREST-ONLY LOANS

In Denmark homeowners have since 2003 had an option to defer principal payments for up to 10 years on mortgage loans with a loan term of 30 years. Today, interest-only loans make up 53% of total private residential lending. Interest-only loans make homeowners more sensitive to declines in housing prices and interest rate fluctuations.

The Supervisory Diamond sets a limit to the proportion of interest-only loans for private residential properties: The proportion of interest-only loans in the LTV bracket above 75% of the lending limit must not exceed 10% of total lending. Interest-only loans are included regardless of their ranking in the order of priority.

Mortgage banks have already launched various measures to incentivise homeowners to amortise their loans. The proportion of interest-only loans will decrease gradually as the homeowners' initial 10-year interest-only periods expire.

LIMITATION OF LENDING WITH SHORT-TERM FUNDING

Over the last 15 years, fixed-rate loans have been partially replaced by adjustable-rate mortgages (ARMs) funded by bonds with maturities of 1-10 years. When the bonds mature, new bonds are issued and sold, and the mortgage rate is reset. In extreme situations, the mortgage system could be facing a refinancing risk as the mortgage banks must sell new bonds regularly to fund existing loans.

Although the number of bonds sold at refinancing auctions has increased during the years, the financial crisis demonstrated that Danish covered bonds can be sold even during times of great uncertainty. Over the last five years, the mortgage sector has spread the January refinancing auctions over April, July and October as well. This has resulted in a more even distribution of the sale of bonds funding ARMs and floating-rate loans. In addition, the total amount of bonds to be refinanced has also decreased.

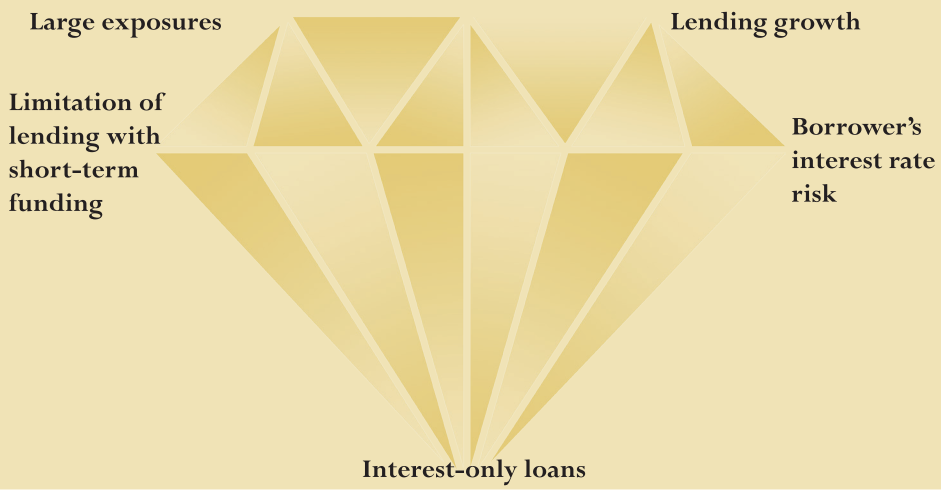
The Supervisory Diamond sets an annual limit to the proportion of lending subject to refinancing: The proportion of lending subject to refinancing must be below 12.5% of total lending on a quarterly basis and below 25% of total lending on an annual basis.

BORROWER'S INTEREST RATE RISK

Today, 63% of all home loans in the market carry a variable rate of interest. This exposes the individual borrower to interest rate risk as the loan rate may rise.

An indicator in the Supervisory Diamond sets a limit to interest rate risk: The proportion of lending where the LTV ratio exceeds 75% of the lending limit and where the loan

Chart 4:
Supervisory Diamond for mortgage banks



Source: Danish FSA

rate is fixed for up to 2 years must be below 25%. This only applies to private homeowners and residential property rental.

It is worth noticing that most Danish homeowners could afford to make the regular principal and interest payments even if interest rates should surge. That is the conclusion of several studies by Danmarks Nationalbank, the Ministry of Business and Growth and others. The studies have been prepared at the level of individual homeowners' loans and specific types of loan.

LENDING GROWTH

The Supervisory Diamond sets a limit to lending growth in individual customer segments of 15% annually. The four segments are private homeowners, commercial property rental, the agriculture sector and other corporate. No mortgage banks currently have lending growth exceeding 15%.

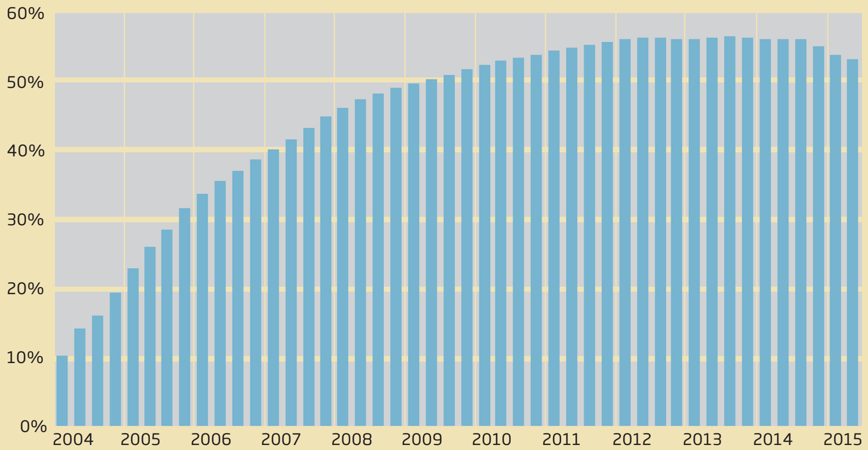
LARGE EXPOSURES

The last indicator in the Supervisory Diamond is a limit to large exposures. The sum of the 20 largest exposures after deductions must be lower than the mortgage bank's Common Equity Tier 1 (CET1) capital.

MAKING THE MORTGAGE SYSTEM EVEN MORE SECURE

The Danish mortgage system is strong compared to other methods of financing. The high level of security has boosted demand for Danish covered bonds – also during the crisis. The system has proved robust in times of crisis because its structure involves very low risk. In the opinion of the Association of Danish Mortgage Banks, the Supervisory Diamond makes the Danish mortgage system even more robust, for the benefit of homeowners and businesses.

Chart 5:
Proportion of homeowners with interest-only loans



Source: Association of Danish Mortgage Banks

Focus on better EU regulation

The financial sector has seen a wide range of new legislation from the EU in recent years. Capital adequacy rules in the CRR and CRD IV, increased requirements for securities trading in MiFID II, rules to combat money laundering and market abuse and much more have been introduced in the wake of the financial crisis. However, the pendulum is about to swing in the opposite direction. Following the barrage of rules in recent years, political focus on the extensive regulation has increased in the EU and in Denmark.

The European Commission proposed in spring 2015 a package of initiatives intended to improve the quality of EU legislation in the coming years. The proposals are about increased stakeholder engagement, from planning to implementation of proposals. Another objective is improved assessment of the expected consequences of EU legislation.

The Danish Minister for Business and Growth is chairing a government committee charged with ensuring a more systematic implementation of new EU rules so as to avoid 'over-implementation', including any unduly restrictive rules to the detriment of Danish businesses and jobs. The government has furthermore announced that it will set up an implementation council with members from trade organisations, experts etc. The council will advise on the implementation of EU legislation aimed at the business sector.

The Association of Danish Mortgage Banks welcomes these initiatives. We see them as an acknowledgement by politicians that extensive and detailed regulation comes at a price. That regulation could potentially obstruct an agenda for growth and prosperity in Denmark and the EU. But the good intentions should be backed by action. We need to see an effect of the increased focus on better regulation.

DETAILED REGULATION IS FLYING UNDER THE POLITICAL RADAR

Mortgage banks and other financial undertakings are currently struggling to implement vast amounts of technical legislation in all parts of their business. The bulk of it derives from the EU. In fact the legislation discussed by the European Parliament and the Council is only the tip of the iceberg.

The European Commission has the power to adopt additional rules. When the regulatory process is completed at the political level (level 1), EU officials take over at level 2. The relationship between level 1 and level 2 legislation resembles the relationship between acts and executive orders in Denmark. However, compared with Danish executive orders, level 2 legislation contains an unprecedented amount of detailed regulation of the sector.

For example, the rules at product level applicable to investment products. In this area, businesses must identify target groups of each individual product:

"When manufacturing products, the firm shall identify the potential target market for each product and be able to specify the type(s) of client for whose needs, characteris-

[2] Final report: ESMAs Technical Advice to the Commission on MiFID II and MiFIR, s. 57

tics and objectives the product is compatible. As part of this process, the firm shall identify any groups of investors for whose needs, characteristics and objectives the product is not compatible. (…)"

Mortgage banks are subject to the rules on investment products as bonds are purchased and sold when a mortgage loan is issued. Thus, the mortgage banks must define who belong to the target group of mortgage loans and who do not. This is considered a step backwards compared to the current practice, where the decision whether or not to grant a loan is based on a thorough examination of the individual customer's situation.

This example may not seem that invasive at first glance. But the businesses must develop, implement and evaluate the processes. They must document their work and keep records to disclose to the authorities on request. It involves a lot of administrative work to fulfil some rules the usefulness of which may well be questioned. And the expenses for this administrative work will ultimately be paid by the customers.

MORE POLITICAL CONTROL, PLEASE

There is room for improvement considering the objective of better regulation. It is imperative to strike a better balance between reasonable regulation of the sector and the desire to create growth and prosperity in Denmark and the EU. Politicians should to a greater extent reclaim the power and responsibility through increased control by the Danish parliament. Especially regarding the detailed regulation which the financial undertakings are currently working hard to comply with.

Modernisation of rules and less bureaucracy

Legislators in both the EU and in Denmark continually introduce new requirements for businesses. In the financial sector, the amount of new requirements has been substantial in the years after the financial crisis. All these new requirements involve costs for the businesses and ultimately for customers.

The Association of Danish Mortgage Banks is working on minimising the cost for customers and has therefore taken various initiatives to achieve reductions and savings in other areas. The Association has made a targeted effort to have some of the rules removed that make it more expensive for customers without adding any value, for example because they have been outmatched by new technology.

ANNOUNCEMENT OF FORCED SALES NOW ONLINE

Until 1 January 2015, the law dictated that forced sales by public auction should be announced in daily newspapers. In the opinion of the Association, there was every reason to abolish the statutory printed announcements and instead use the option of announcements on the Internet as is well-known in connection with open market home sales. It would attract more potential buyers and thereby increase the prices of the properties sold at forced sales. Against this backdrop, the Association urged the Ministry of Justice to modernise the rules for announcement of forced sales.

The rules have now been modernised, and the result is better and cheaper announcements for the benefit of homeowners who are forced to sell their homes and who – ultimately – pay all the costs of the auction. Previously, an announcement could easily cost as much as DKK 10-15,000 or more per auction. Now, making an announcement on the Internet costs a fraction. Thus, homeowners who have to sell their homes at a forced sale now pay less to get out of their unfortunate circumstances.

FORCED SALES COULD BE SIMPLER AND CHEAPER

The Association has called on the Ministry of Justice to revise the rules on forced sales so that execution need not be levied upon mortgage default. In our opinion, the mandatory levy of execution based on mortgages is unnecessary and it add costs to the forced sale without adding value. Mortgage banks should be able to apply for a forced sale directly on the basis of the mortgage.

Today, execution also serves to prolong the processing time at the enforcement courts. Mortgage banks, their attorneys as well as the enforcement courts can save time if the Association's proposal, which is being reviewed by the Standing Committee on Procedural Law and the Ministry of Justice, is adopted.

NEW CALCULATION METHOD FOR MORTGAGE REGISTRATION FEES CAN SAVE THOUSANDS OF WORKING HOURS

In the opinion of the Association, the Danish Act on mortgage registration fees is unduly complicated and should be thoroughly modernised. A new method to calculate the mortgage registration fees would save thousands of man hours in the financial sector. The Association is working to have the rules revised for the purpose of simpler and easier calculation of the fees.

CVR NUMBERS FOR PUBLIC HOUSING ESTATES COULD MAKE ELECTRONIC LAND REGISTRATION EASIER

Access to electronic land registration, which was introduced in September 2009, requires a unique identifier in the form of either a CVR (central business register) or a CPR (civil registration) number. This is to ensure that each mortgage is uniquely linked to a debtor. The system presupposes that all entities have either a CVR or a CPR number. But public housing estates do not, as they are not separate legal persons, and so far they have not been assigned CVR numbers. We have urged the authorities for years to find a legally viable way to assign CVR numbers to public housing estates.

Mortgage banks and public authorities spend many resources on identifying and handling public housing estates outside the established system. The Association will continue its efforts to solve this problem.

Lending activity

Lending activity in the mortgage market in 2014 and the first half of 2015 was characterised by remortgaging by homeowners.

Lending has moved away from loans with 1-year interest rate reset (the so-called F1 loans) and deferred amortisation, while the amount of fixed-rate loans and other floating-rate loans has grown. Total mortgage lending has seen modest growth in the past year. Outstanding mortgage loans totalled DKK 2,566bn in Q2/2015, a rise of DKK 39.9bn on a year earlier.

In H1/2015, principal payments and prepayments amounted to DKK 353bn, reflecting especially the great demand for remortgaging, see Chart 6. Activity is at the highest level for 12 years. In comparison, principal payments and prepayments amounted to DKK 128bn in H1/2014.

HOMEOWNERS

Outstanding lending for owner-occupied dwellings and holiday homes has increased by an aggregate DKK 25.9bn over the past year to DKK 1,471bn. The increase breaks down into DKK 73bn of fixed-rate loans, DKK 33bn of loans subject to semi-annual refinancing, and DKK 30bn of loans with 2-10-year interest rate reset periods (the so-called F2-F10 loans). Conversely, loans with 1-year interest rate reset have dropped by DKK 81bn and capped loans by DKK 29bn, see table 1.

The increase in fixed-rate loans in recent quarters is the result of not only more new loans, but also the fact that homeowners have increased their debt upon remortgaging. In H1/2015 a quarter of the increase in fixed-rate loans was due to more new loans, and three in four new loans for home purchases were fixed-rate loans. Fixed-rate loans make up 37% of total outstanding private residential mortgage lending. A year ago, their share was 32%, see Chart 7.

INTEREST-ONLY LOANS

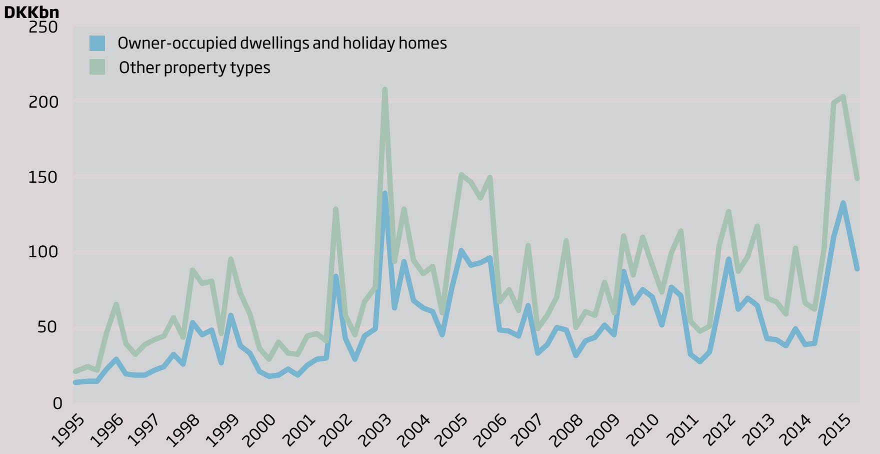
The share of interest-only loans for homeowners has dropped from 56% a year ago to 53% in Q2/2015. Interest-only loans with 1-year interest rate reset have seen the greatest reduction. Over the past year, the amount of interest-only loans with 1-year interest rate reset has declined by DKK 59bn, while capped interest-only loans have declined by DKK 19bn. In the same period, uncapped floating-rate interest-only loans have increased by DKK 22bn, interest-only loans with 2-10-year interest rate reset have increased by DKK 20bn, and fixed-rate interest-only loans by DKK 7bn.

COMMERCIAL AND OTHER LENDING

In Q2/2015 mortgage banks' outstanding mortgage lending for agriculture, industry/trades, office/retail, subsidised housing, private rental properties and other properties totalled DKK 1,095bn. Lending to these sectors has grown by DKK 14bn in the past year, the main reason being a rise in lending for subsidised housing and private rental properties.

Chart 6:

Principal payments and prepayments on mortgage loans by property type



Source: Association of Danish Mortgage Banks

Table 1:

Outstanding lending for owner-occupied dwellings and holiday homes by loan type

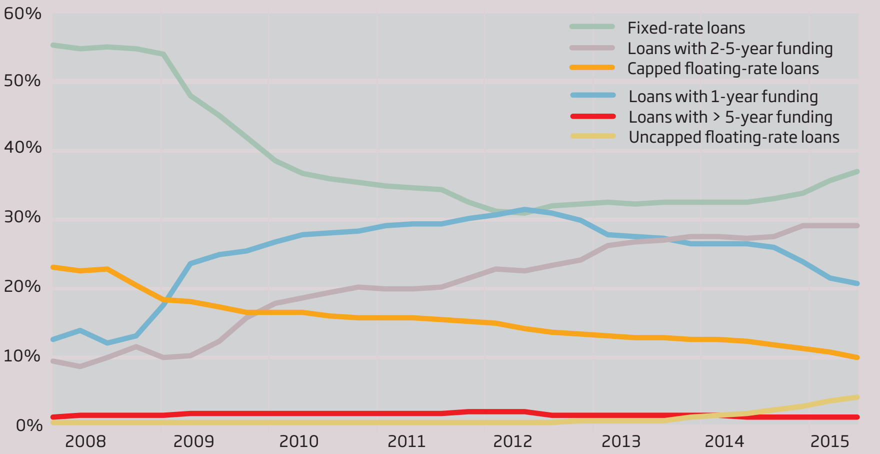
DKK bn	Q2/2014	Q3/2014	Q4/2014	Q1/2015	Q2/2015	Change QoQ	Change YoY
Loans with 1-year funding	379	369	340	307	299	-8	-81
Loans with 2-5-year funding	390	394	415	419	422	2	31
Loans with 6-10-year funding	15	15	15	15	14	-1	-1
Fixed-rate loans	466	472	483	515	538	23	73
Capped floating-rate loans	172	167	158	150	143	-7	-29
Uncapped floating-rate loans	23	29	37	49	56	7	33
Total	1,445	1,446	1,447	1,455	1,471	16	26

Source: Association of Danish Mortgage Banks

Chart 7:

Share of outstanding lending for owner-occupied dwellings and holiday homes by loan type

Note: Loans were reclassified in Q3/2012. An amount equivalent to about DKK 9.5bn was reclassified from ARMs and floating-rate (interest-only) loans to fixed-rate loans.



Source: Association of Danish Mortgage Banks

Property market

Prices of houses and owner-occupied flats are on the rise, and the number of home sales is higher than a year ago in all Danish regions.

In Q1/2015 house and flat prices were 5.7% and 9.6% higher, respectively, than in Q1/2014, see Charts 8 and 9. House prices have gone up in all regions compared with last year. According to the housing price statistics of Statistics Denmark, prices also rose in the first two months of Q2/2015.

At the same time, the number of home sales is higher than a year ago in all Danish regions. House sales in Q1/2015 were 22% higher than in the same quarter in 2014, and the sale of flats was 36% higher. The sales activity for houses at national level matches the average for the last ten years.

HOUSING SUPPLY

In July 2015, 58,776 houses, holiday homes and owner-occupied flats were listed for sale by estate agents, and this is some 5,300 fewer than a year ago, see Chart 10. Even though the supply of houses has declined over the last three years, there is still a large number of homes for sale as the supply has declined from a high level. The situation is different for flats. The total supply of flats has more than halved compared with eight years ago when the supply of flats peaked.

TIMES-ON-MARKET

In Q1/2015 it took eight months on average to sell a detached or terraced house, see Chart 11. The time-on-market for houses has declined by four days since the beginning of 2014. The time-on-market for flats has declined by 15 days. In the same period, the time-on-market for holiday homes has risen by 14 days. In Q1/2015, it took an average of five and 12 months, respectively, to sell a flat and a holiday home.

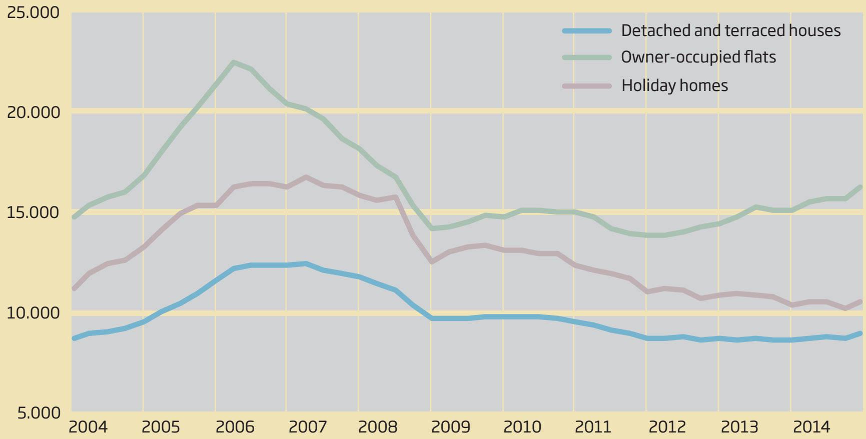
ARREARS

In Q2/2015 the arrears ratio was 0.27%, meaning that for each DKK 100 of mortgage payment due, DKK 0.27 was still outstanding. During the economic downturn in the early 1990s, the arrears ratio was around 2.5%, see Chart 12. Today's low arrears ratio should be viewed against a relatively low unemployment rate and the very low interest rate level. This means that most homeowners can afford their mortgage payments and thereby avoid falling into arrears.

FORCED SALES

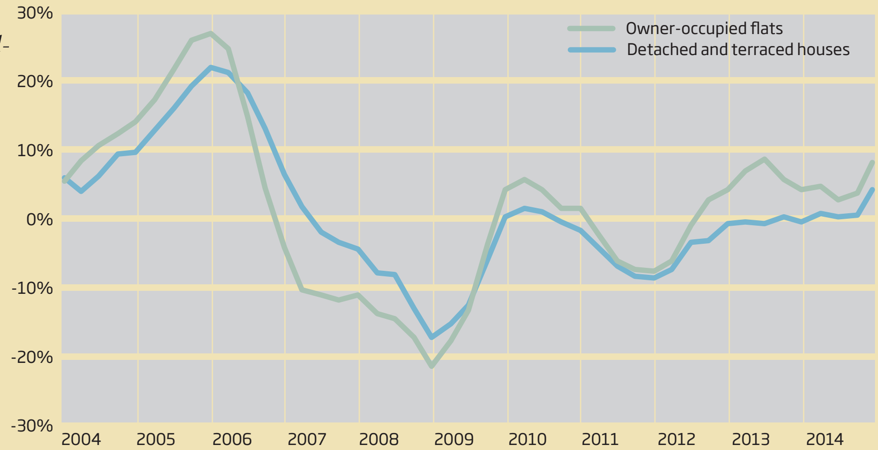
The first seven months of 2015 saw 2,052 forced sales. This corresponds to a monthly average of 293. The number of forced sales generally varies from one month to the next, but 2015 has seen the same level as in 2014. During the crisis in the 1990s, the monthly average topped 1,200, see Chart 13.

Chart 8:
Prices of owner-occupied dwellings across Denmark, 2004-2015, DKK/sqm



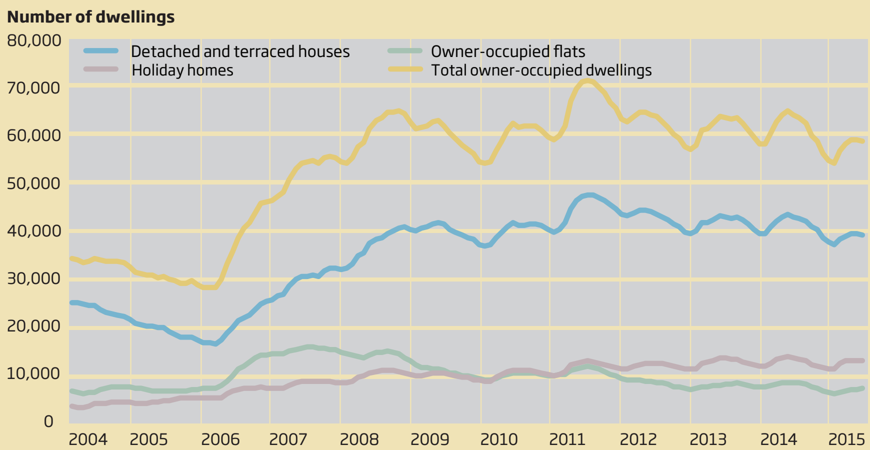
Source: Housing Market Statistics

Chart 9:
Prices of owner-occupied dwellings across Denmark (annual increase), 2004-2015



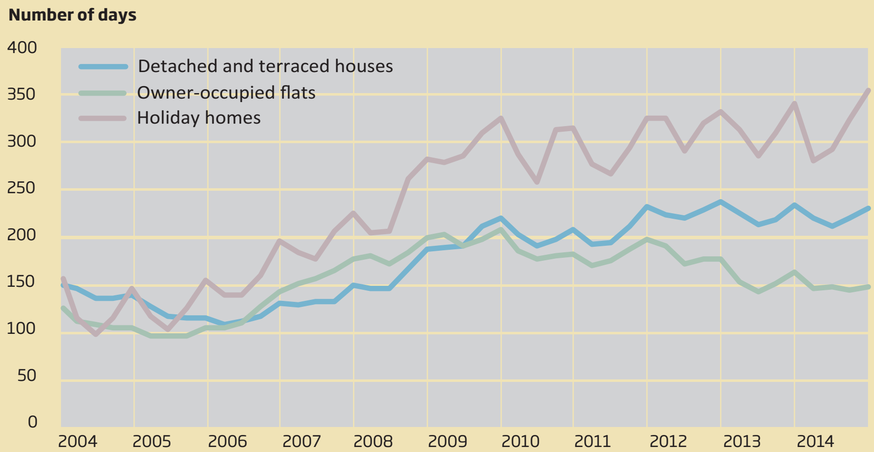
Source: Housing Market Statistics

Chart 10:
Owner-occupied dwellings for sale, 2004-2015



Source: Association of Danish Mortgage Banks

Chart 11:
Times-on-market across Denmark



Source: Association of Danish Mortgage Banks

Chart 12:
Arrears ratio for outstanding mortgage lending for owner-occupied dwellings and holiday homes, 1991-2015

Note: The arrears ratio indicates the proportion of total mortgage payments that remains unpaid 105 days past the due date.

Source: Association of Danish Mortgage Banks

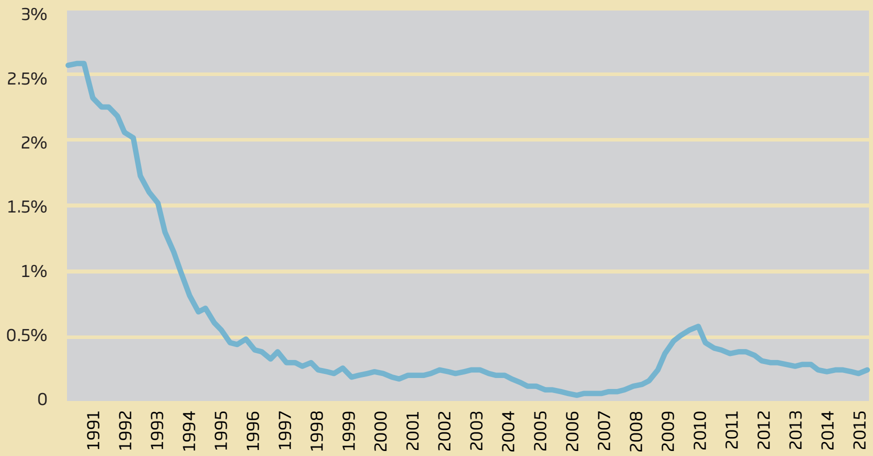
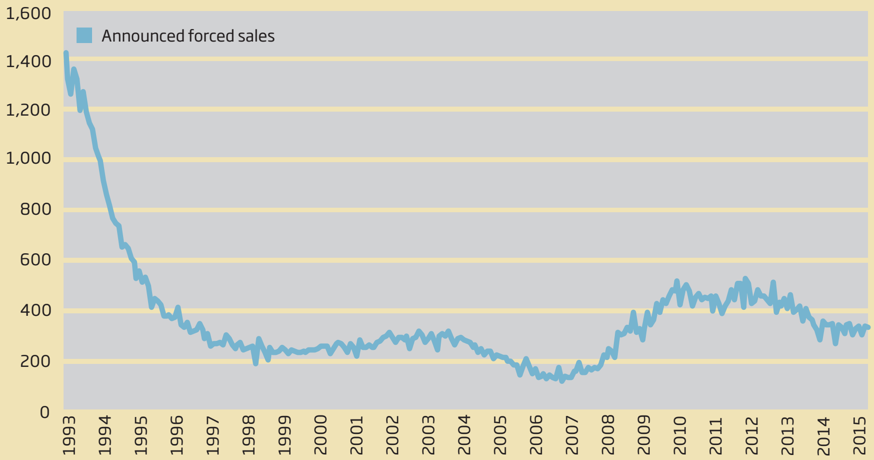


Chart 13:
Total forced sales of detached and terraced houses (seasonally adjusted), 1993-2015

Source: Statistics Denmark



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The Association of Danish Mortgage Banks (4)

Deputy Director Peter Jayaswal,
The Association of Danish Mortgage Banks (1)

The Association of Danish Mortgage Banks has a secretariat of around 27 employees. The secretariat is organised into specialised departments and has an EU-based representative office in Brussels. Head of the secretariat is Ane Arnth Jensen, Director General.

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