

# Nykredit Group

## H1/2016 financial results call

CFO/CRO Group Managing Director  
Søren Holm

18 August 2016



**Nykredit**

# Highlights from H1/2016

## Business results

- Profit from core business up 3% compared to H1/2015, excluding contribution to the Danish Resolution Fund
  - Top-line normalised compared to record high H1/2015 – down 7%
  - Costs reduced according to plan
  - Loan loss provisions almost zero due to increasing property prices and economic growth
- Negative value adjustments for swaps amount to DKK 1,312m
- Guidance for full year profit from core business revised up by DKK 500m to DKK 5-5.5bn

## Business units

- Totalkredit lending increased by DKK 5.3bn despite run-off of Jyske Bank portfolio
- Total mortgage lending decreased DKK 5.9bn compared to end-2015
- Bank lending and deposits increased by 5% and 10% respectively compared to end-2015
- Increase in Assets under Management in Wealth Management

## EBA stress test

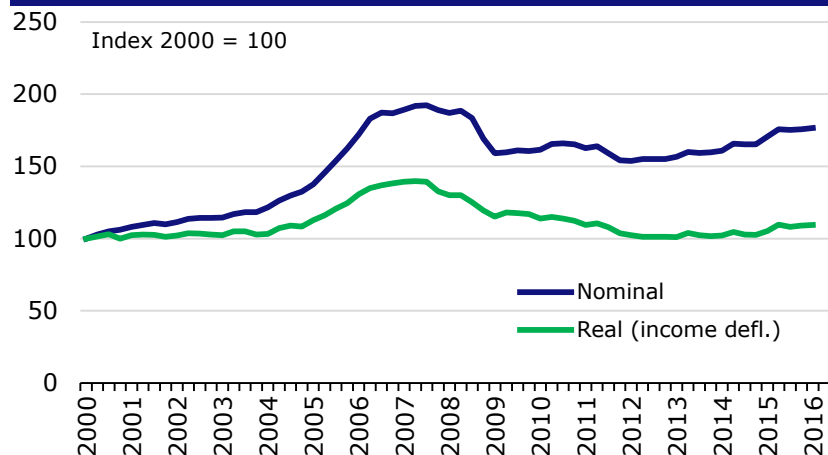
- Result of stress test shows that Nykredit will have CET1 of 14.2% in severe adverse scenario

## Ratings

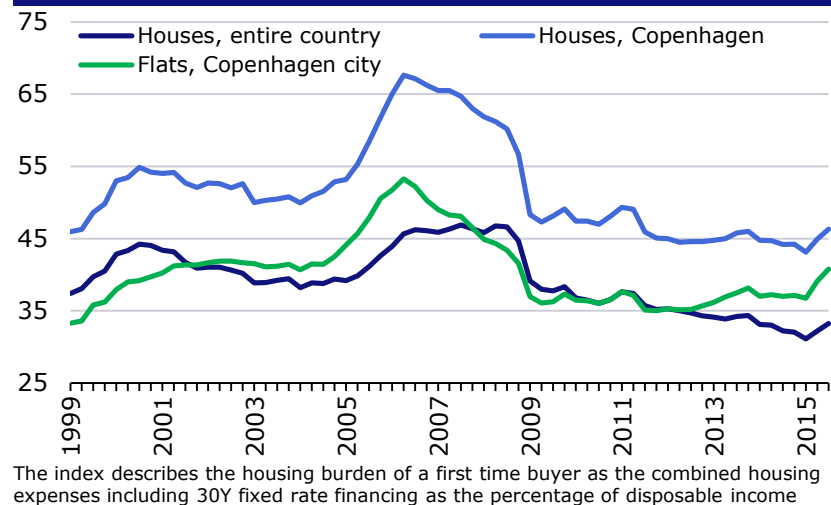
- S&P revises outlook for Nykredit's senior rating to "Stable" from "Negative"

# Danish housing market recovering

## House price inflation, Denmark



## Housing burden, % of disposable income

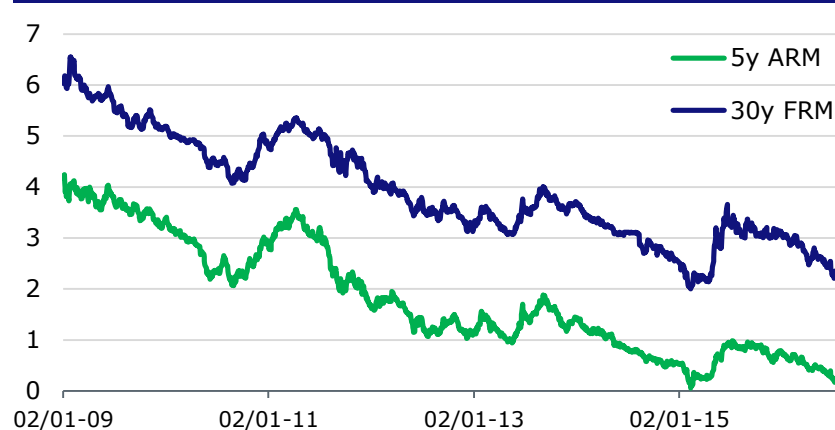


## Danish economy and household finances

- GDP growth expected at approx. 1.0% in 2016 and 1.4% in 2017
- Household fundamentals are strong, but consumption will grow moderately due to continued focus on bringing down debt
- Real house prices are recovering – primarily in and around major cities
- Low and falling interest rates support the property market

Source: Macrobond, Nykredit Markets, Statistics Denmark, cover pool

## DKK covered bond rates, % p.a.



## Profit from core business up 3%

### Excluding contribution to Danish Resolution Fund

DKKm	2015	H1/2015	H1/2016	Index
Core income from business operations	11,945	6,236	5,825	93
Securities and debt (senior and subordinated)	(572)	(343)	(211)	62
<b>Income from core business</b>	<b>11,373</b>	<b>5,893</b>	<b>5,614</b>	<b>95</b>
Operating costs, depreciation and amortisation	5,005	2,420	2,366	98
Danish resolution fund	61	-	69	-
<b>Core earnings before impairment losses</b>	<b>6,307</b>	<b>3,473</b>	<b>3,179</b>	<b>92</b>
Impairment losses on loans and advances	920	449	125	28
<b>Core business earnings after impairment losses</b>	<b>5,387</b>	<b>3,024</b>	<b>3,054</b>	<b>101</b>
Value adjustments of derivatives due to interest rate chg.	685	864	(1,388)	-
Other value adjustments of interest rate swaps	(275)	(410)	76	-
Goodwill adjustments	1,965	-	-	-
Investment portfolio income	853	491	533	109
<b>Profit before tax</b>	<b>4,685</b>	<b>3,969</b>	<b>2,275</b>	<b>57</b>
AT1 interest payable classified as dividend	197	80	116	-
Value adjustment of strategic equities against equity	7	306	(157)	-

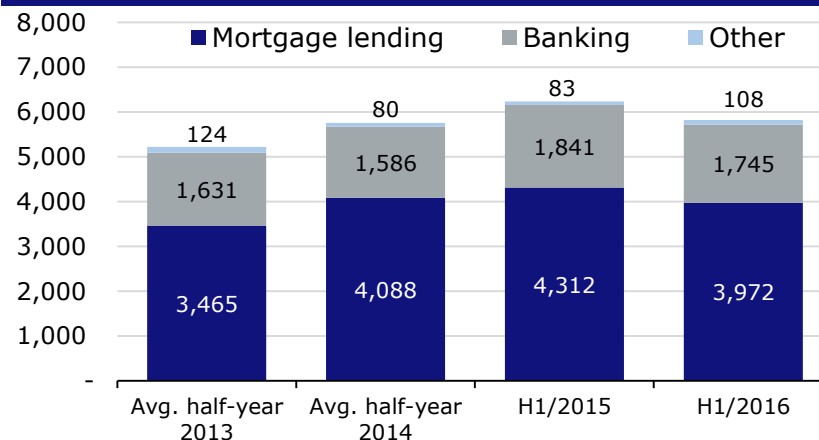
Source: Nykredit H1/2016 report

# Profit from core business forecast revised upwards

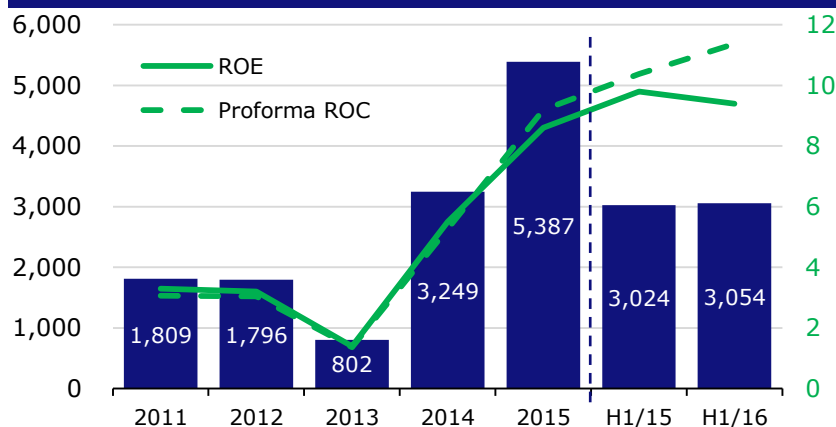
## Revised earnings guidance

- In the Q1/2016, Management's forecast of profit from core business was DKK 4.5bn-5.0bn for 2016
- In the H1/2016 Report full-year profit guidance revised upward by DKK 0.5bn to around DKK 5.0bn-5.5bn

## Core earnings from business operations, DKKm



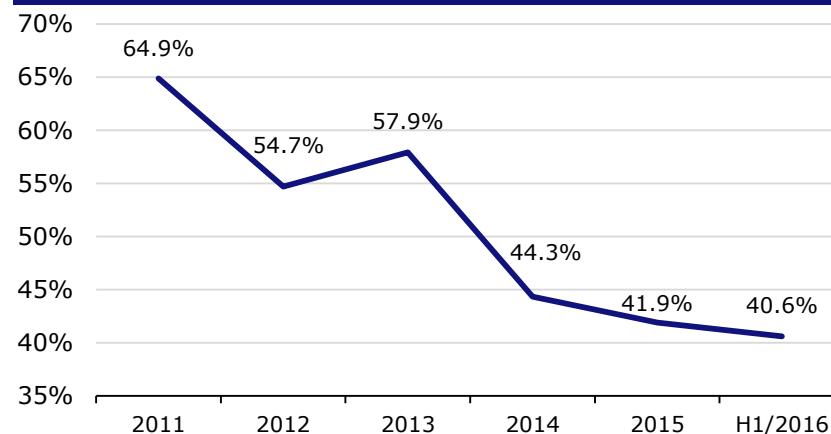
## Profit from core business, DKKm, % avg eqt



RHS: Profit from core business, % pa of avg. equity or % pa of 17.5% of avg. REA

Source: Nykredit H1/2016 report

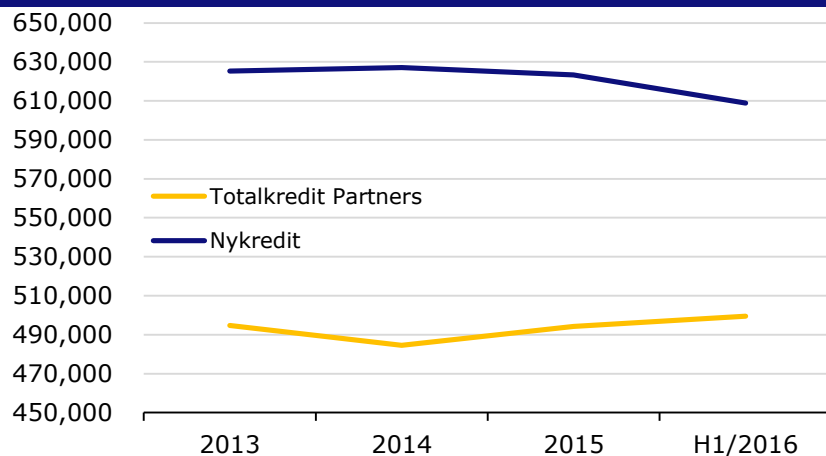
## Group cost:income ratio



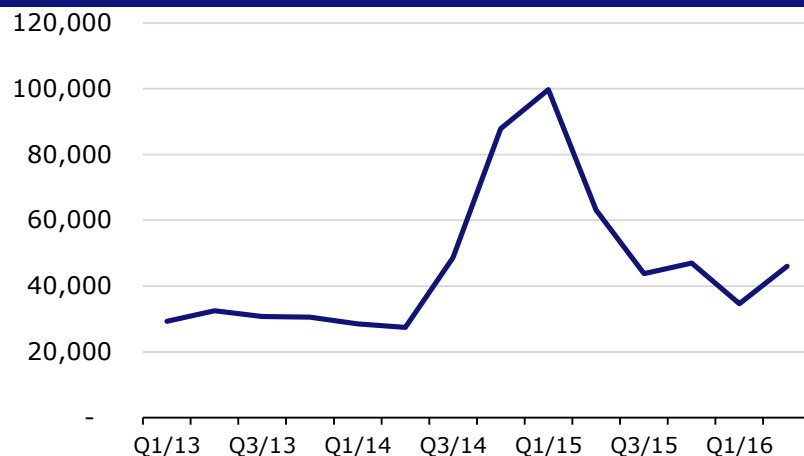
Note: Operating costs, depreciation and amortisation, excl special value adjustments as % of core earnings from business operations

# Normalised new lending but growing business volume

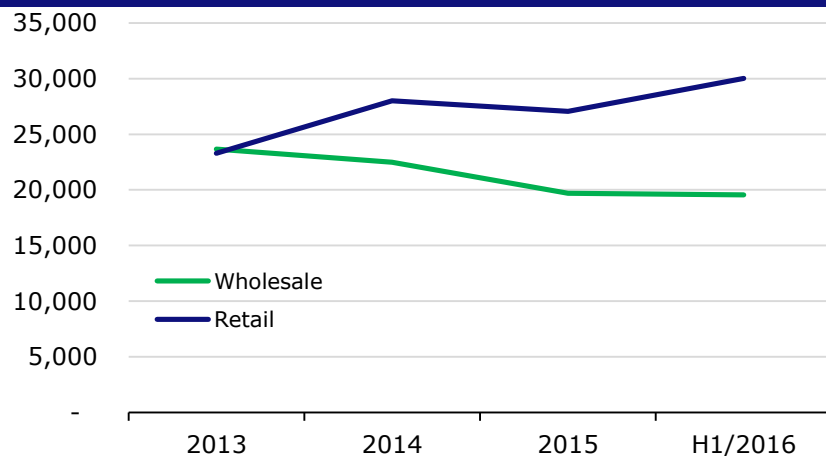
## Mortgage lending (portfolio), DKKm



## Gross new mortgage lending, DKKm



## Bank lending (portfolio), DKKm



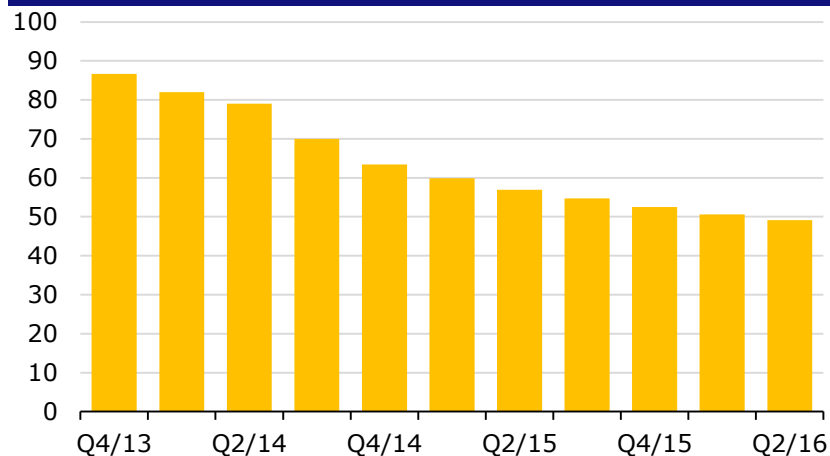
## Comments

- Mortgage lending in Totalkredit increased by DKK 5.3bn despite run off of Jyske Bank portfolio
- Extraordinary high gross lending in H1/2015 due to low 30-year mortgage rates. More normal level in H1/2016
- Bank lending to Retail clients increasing compared to H1/2015. Commercial lending declining.
- Deposits from both Retail and Commercial clients growing despite negative interest rate environment
- Pass-through mortgage funding model insulates Nykredit from margin pressure due to falling interest rates

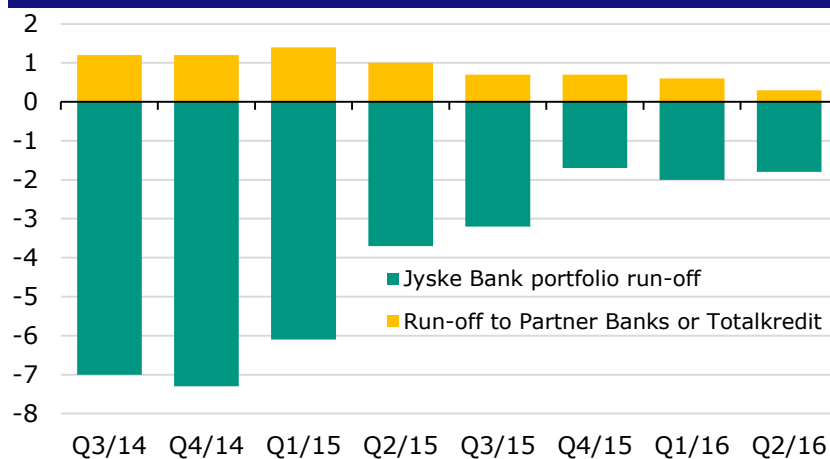
Source: Nykredit reports

# Run-off on Jyske Bank portfolio

**Loans originated by Jyske Bank, DKKbn**



**Distribution of run-off, DKKbn**



Source: Nykredit reports



## Comments

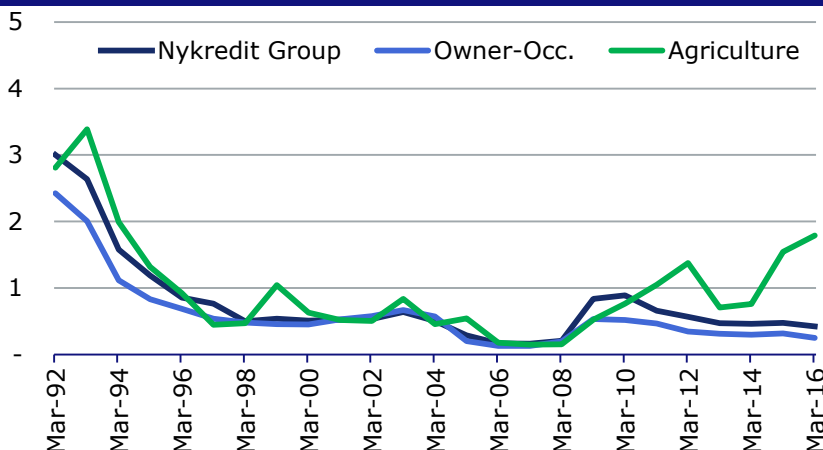
- DKK 48bn of the original DKK 87bn has been redeemed
- As of end-June 2016 DKK 9bn has been captured by partner banks and Totalkredit
- Net run-off on the Jyske Bank portfolio totals DKK 39bn

# Arrears ratios improving - except for agriculture

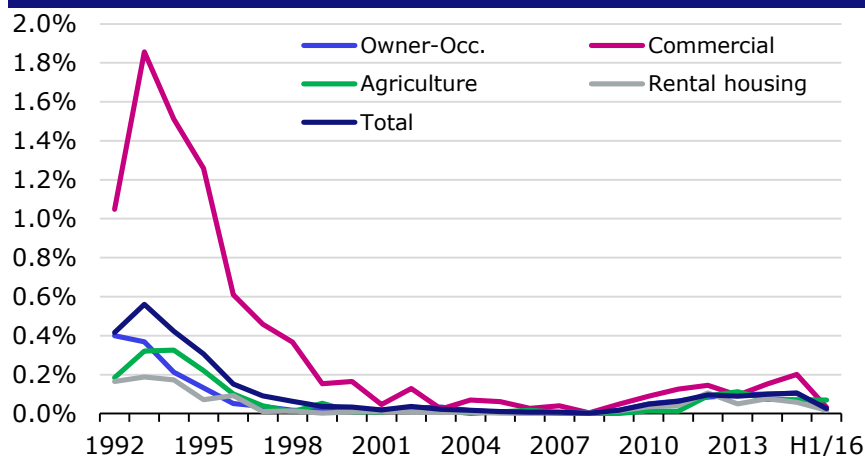
## Mortgage lending: Indexed LTVs (current house prices)

	0-40%	40-80%	> 80%	Avg LTV	Share
Residential	46.0%	28%	2.7%	<b>70.6%</b>	<b>76.7%</b>
Commercial	9.9%	2.5%	0.1%	<b>51.4%</b>	<b>12.6%</b>
Agriculture	6.5%	2.4%	0.2%	<b>58.1%</b>	<b>9.1%</b>
Other	1.3%	0.3%	0.0%	<b>51.0%</b>	<b>1.6%</b>
<b>Total</b>	<b>63.8%</b>	<b>33.2%</b>	<b>3.0%</b>	<b>65.2%</b>	<b>100.0%</b>

## 75-day arrears, %

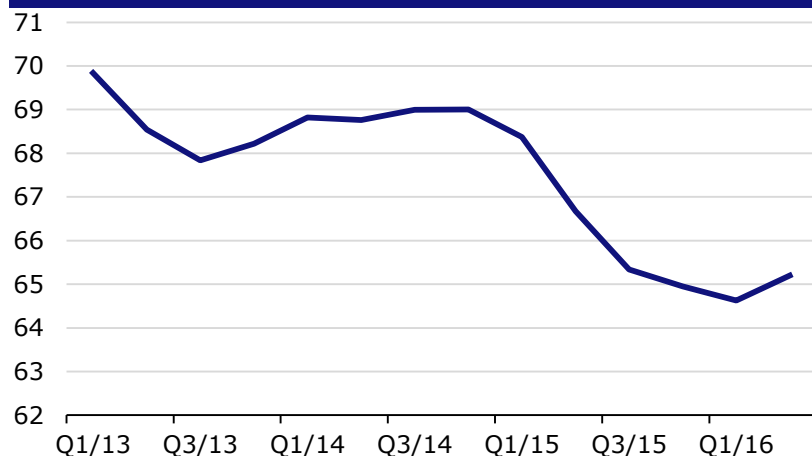


## Mortgage lending: Incurred loss as % of debt



The LTV is calculated on the basis of the top LTV bracket for the loans granted  
Source: Nykredit H1/2016 Report, Cover Pool disclosure reports

## Avg. LTV for Nykredit's owner-occupied lending





# Conservative Group CVA and impairment provisions

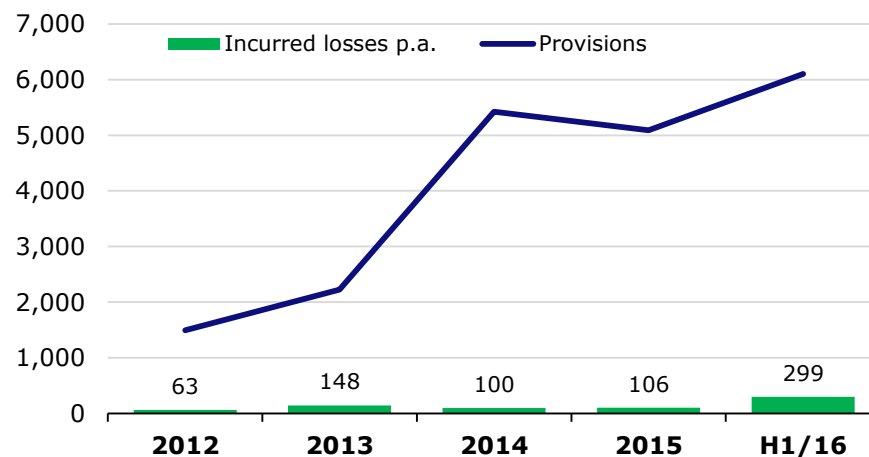
- Credit Value Adjustments on swaps with customers
  - Falling interest rates lead to larger unsecured claims on weak customers
  - Conservative internal policy and valuation guidelines regarding rental housing and cooperative housing associations, including swap exposures
  - Legal risk related to Nykredit's claim against cooperative housing associations with swaps
  - The Supreme Court ruling in May 2016 will not affect Nykredit's impairment provisions, as bankruptcy risk in the cooperative housing sector is already factored in
- CVA provisions are sensitive to changes in the long swap rate
  - 100 bp change in swap rates leads to approx. DKK 1.9bn change in CVA provisions

## Fixed-rate swaps and step-up interest derivatives

H1/2016 DKKbn / %	Negative market value	Total impairment provisions*	Impairment provision, % of market value
Housing cooperatives	8.7	4.6	53%
Agriculture	1.3	0.4	28%
Other	9.4	1.0	11%
<b>Total</b>	<b>19.6</b>	<b>6.1</b>	<b>31%</b>

\* Individual value adjustments, management judgement and CVA

## Swap provisions and incurred losses, DKKm



Source: H1/2016 Reports of Nykredit Realkredit and Nykredit Bank, Fact Book

# Impairments and cover ratio reflect low risk mortgage business

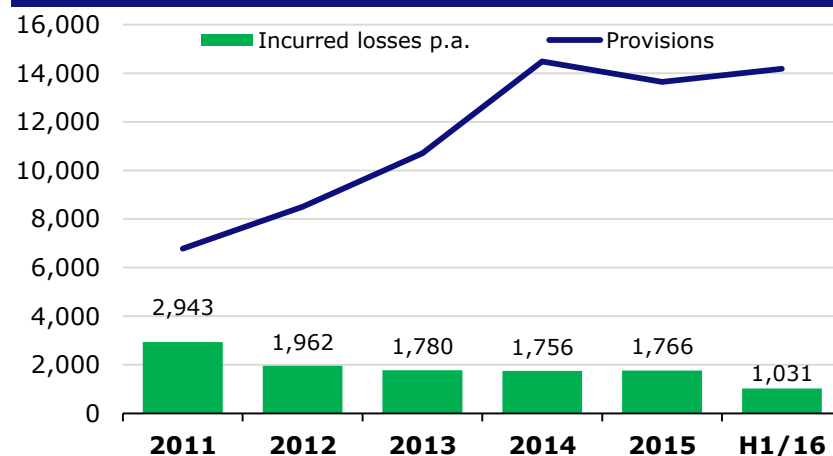
	2012	2013	2014	2015	H1/16
<b>Impairment losses on loans and advances</b>					
- Mortgage, DKKm	1,592	2,415	2,132	1,041	211
- Mortgage, % of stock	0.14	0.21	0.19	0.09	0.02
- Bank, DKKm	557	349	219	(121)	(86)
- Bank, % of stock	0.59	0.29	0.22	(0.12)	(0.10)
<b>Group non-performing loans, %</b> (75 days arrears for mortgage loans) (25-90 days arrears for bank loans)	2.24	2.46	2.39	2.45	2.34
<b>Coverage ratio, %*</b>	26.9	29.1	32.0	28.9	28.8

## Comments

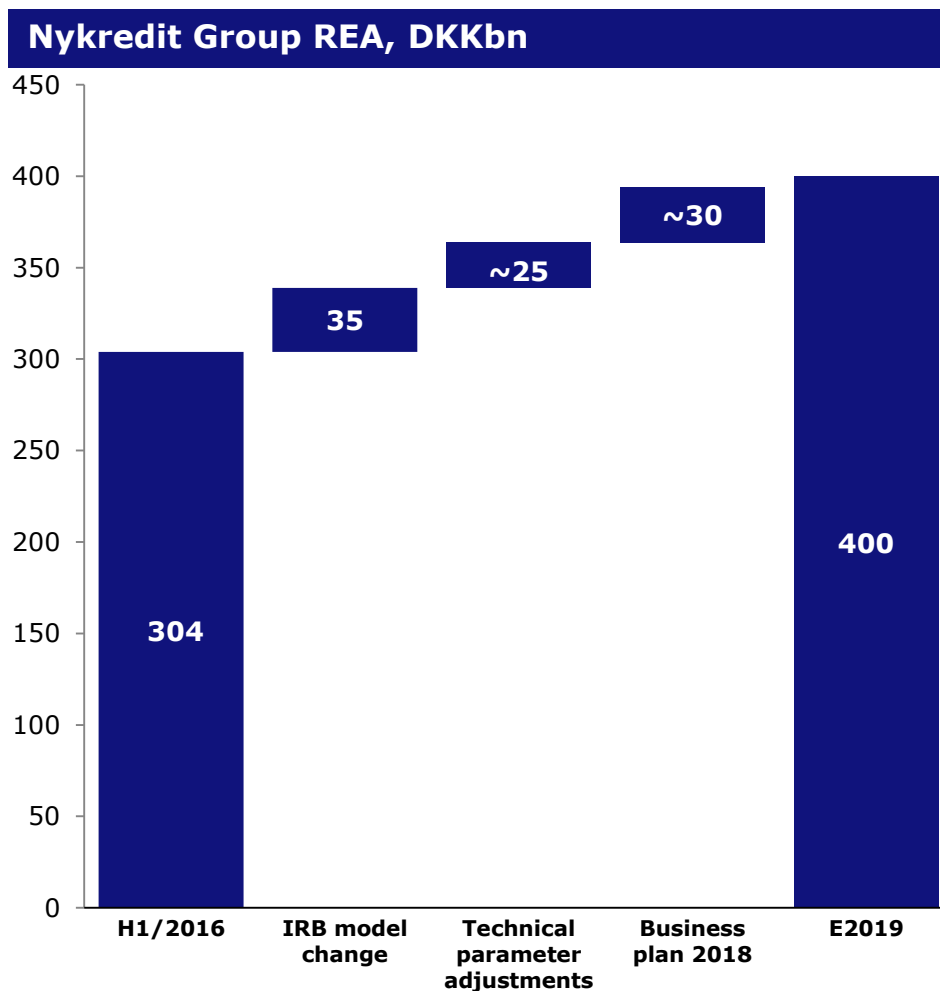
- Foreclosures are at a very low level
- Nykredit has financed 650,000 properties and has only a portfolio of 127 properties acquired by foreclosure compared to 159 in H1/2015
- 85% of the Group risk exposure relates to credit risk, while market risk and operational account for 9% and 6% respectively

\* Reserves for impaired loans / impaired loans  
Source: Nykredit H1/2016 Reports and Fact Book

## Total provisions and incurred losses, DKKm



# Development in Risk Exposure Amount



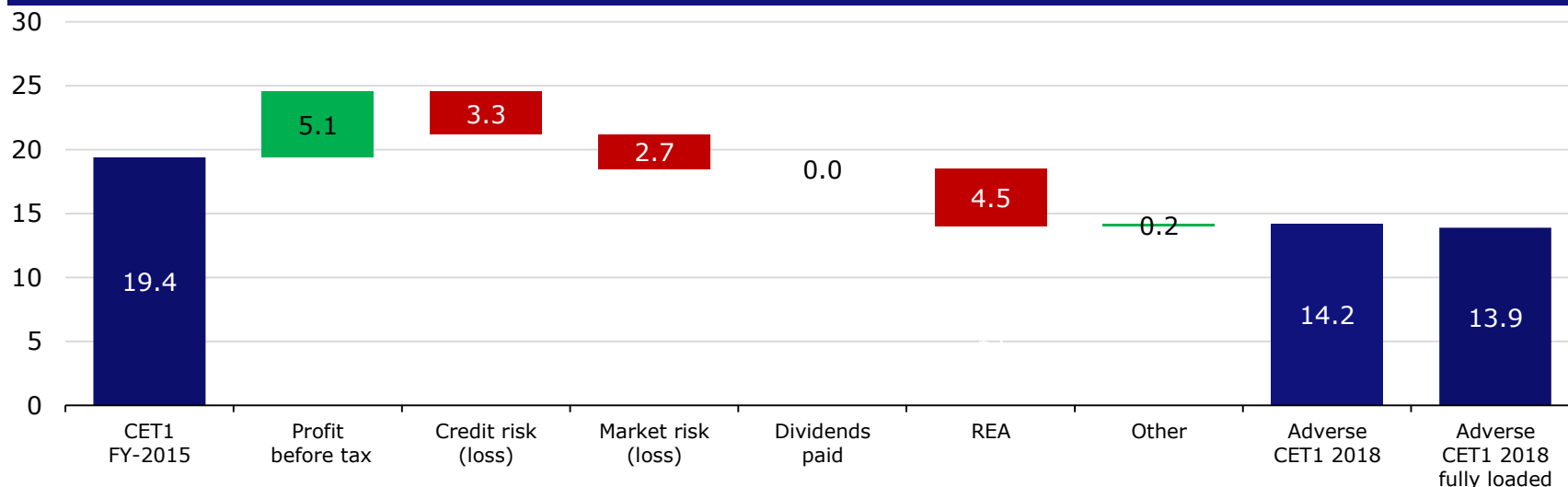
Source: Nykredit H1/2016 Report

## Expected REA adjustment until 2019

- The Nykredit Group's total REA amounted to DKK 304bn at H1/2016.
  - Higher property prices result in lower REA due to lower LTVs
  - Markets risk reduced prior to Brexit referendum
- A number of adjustments to Nykredit's models are currently awaiting the approval of the Danish FSA. Upon approval, REA will increase by an estimated DKK 35bn, resulting in total REA of DKK 339bn. The increase primarily relates to the mortgage business.
- To this should be added adjustments to the detailed capital requirement calculations, resulting in part from the loss experience in the wake of the financial crisis. These adjustments are expected to add another DKK 25bn to REA, leading to a total of approx DKK 365bn.
- Business Plan 2018 is expected to increase REA by another DKK 30bn towards 2019. Estimate is sensitive to property price development. Altogether, the capital requirement, measured by REA, will amount to an estimated DKK 400bn in 2019.
- Capital policy revised annually

# Drivers of Nykredit's EBA stress test results

## Main drivers of changes in CET1 ratio (transitional, % REA)



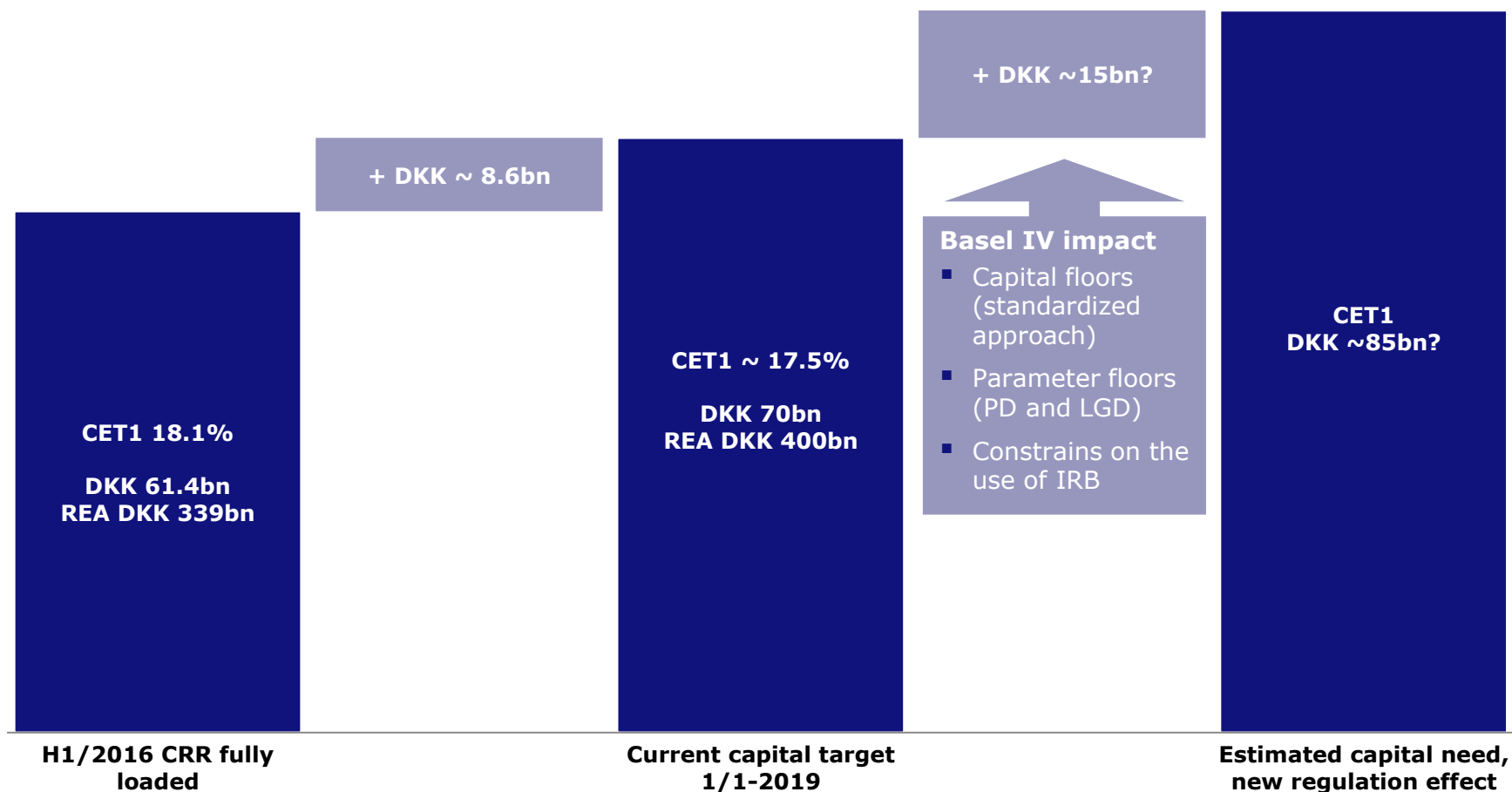
## Nykredit exhibits 14.2% CET1 even in adverse 2018 scenario

- The adverse scenario results in a relatively large decline in Nykredit's CET1 of 526 bp driven by
  - Profit in the stress test is based on historical averages and does not include effect of margin increases
  - Nykredit's predominant mortgage exposure (96% of lending)
  - Very severe stress of property prices with residential properties falling 26% and commercial properties falling 29%
  - Property market stress leads to increases in LTVs and hence increases REA from DKK 325bn to DKK 424bn
  - Technical features of Nykredit's IRB model
  - Market risk driven by Markets operation and CVA on swaps in connection with mortgage business

Source: EBA 2016 stress test data and Nykredit

# Nykredit needs more capital in the longer run

## Nykredit's capital targets and ratios (CRR fully loaded)



Source: Nykredit H1/2016 Report and Fact Book

# S&P revises Nykredit's senior debt outlook to "Stable"

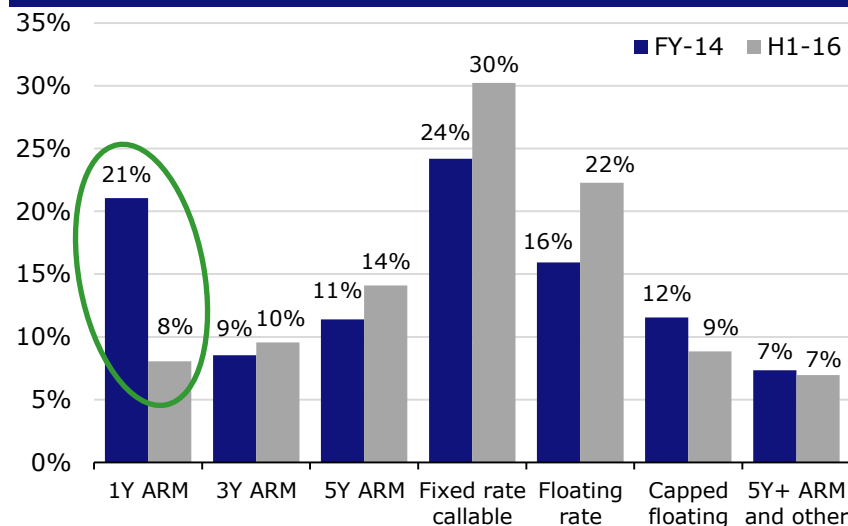
Nykredit ratings	STANDARD & POOR'S	FitchRatings
Covered bonds	AAA	-
Senior unsecured debt	A	A
Short-term debt	A-1	F1
Outlook	Stable	Stable
SRN	BBB+	A
Tier 2	BBB	A-
Tier 2 CoCo	BBB	BBB
Additional Tier 1	BB+	BB+

## S&P review of systemic uplift

- S&P removed 2 notches of systemic uplift from Nykredit's senior unsecured rating...
- ... however the senior unsecured rating was only lowered 1 notch to A due to sufficiently expected ALAC buffers
- Nykredit expects to issue sufficient ALAC-eligible instruments to surpass ALAC threshold of 5% of RWAs to maintain a 1 notch uplift

Source: Nykredit H1/2016 report and Rating reports

## Nykredit loan portfolio composition progress



## Extension of funding profile

- Reliance on 1-2 year funding has been a concern of S&P
- Nykredit has reduced short funding significantly
  - Volume reduced by 1pp in Q2/2016 to 8% of mortgage loan portfolio
  - Nykredit expects to continue reducing short term funding
- Customers are increasingly opting for loans with funding terms longer than 3 years

# Funding

## Funding plans

- Nykredit expects to issue ALAC-eligible instruments for EUR 2bn-2.5bn during 2016 and 2017

EUR 1bn of the ALAC issuance need was completed in June/July 2016

The ALAC instrument (Senior Resolution Notes) is issued out of "OpCo" Nykredit Realkredit A/S

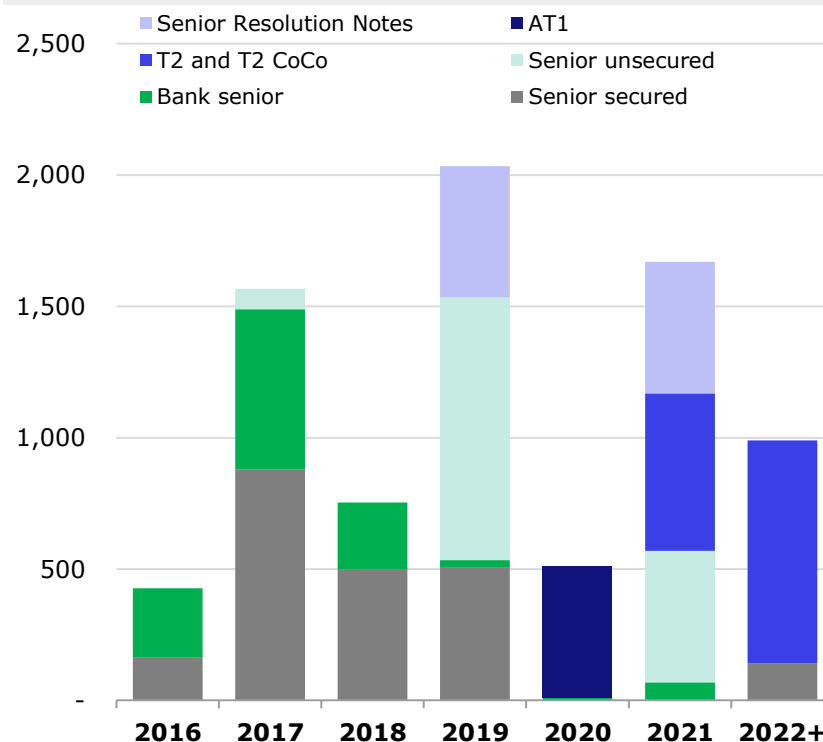
- Contractual loss absorption in resolution
- ALAC eligibility criteria incentivises 3-5 year maturities

- Tap issuance and 4 annual auctions of covered bonds
- On-going interest in the short end of the curve (CP/CD or EMTN)

Source: Nykredit H1/2016 Report

## Nykredit Group maturity profile, EURm

- Profile excluding covered bonds, CP and deposits
- LCR levels end-H1 2016:  
Nykredit Realkredit Group: 226%  
Mortgage institutions: 501%  
Nykredit Bank A/S: 143%







# Nykredit Group – financial ratios

	2012	2013	2014	2015	H1/16
<b>Net interest margin, %</b> - Nykredit Realkredit Group	0.80	0.75	0.82	0.86	0.81
<b>Profit (loss) for the period</b> - As % pa of average equity	4.6	2.9	(0.5)	5.0	5.4
<b>Profit (loss) before tax for the period</b> - As % pa of average equity	5.6	3.3	(0.3)	7.5	6.9
<b>Profit from core business for the period</b> - As % pa of average equity	3.2	1.4	5.5	8.6	9.4
<b>Total assets, DKKbn</b>	1,433.4	1,417.4	1,457.3	1,383.8	1,407.3
<b>Risk Exposure Amount (REA), DKKbn</b>	326.8	346.0	358.6	311.2	304.1
<b>Leverage ratio, %</b>	-	-	-	4.4	4.4
<b>S&amp;P RAC ratio (DEC 2015), %</b>					10.9
<b>Distance to MDA, not fully loaded, DKKbn</b>				38.4	39.9
<b>Distance to MDA, fully loaded, DKKbn</b>				35.6	37.2
<b>Available Distributable Items (ADI), DKKbn</b>				26.2	27.3
<b>Total capital ratio, %</b>	19.1	18.9	18.2	23.9	24.8
<b>CET1 capital ratio, %</b>	15.8	15.8	15.4	19.4	20.2

For the purpose of return on equity, the Additional Tier 1 (AT1) capital raised in H1/2016 is treated as a financial obligation for accounting purposes, and the dividends for the period thereon for accounting purposes are included as interest expenses on subordinated debt in the profit for the year

\* A measure of impaired or doubtful loans (lowest rating category)

\*\* Reserves for impaired loans/impaired loans

Source: Nykredit H1/2016 Reports and Fact Book

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- Publications on markets
- Cover pool data