

# DANMARKS NATIONALBANK

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Some homeowners use deferred amortisation to sustain excessive consumption

## Homeowners reduce consumption when the non-amortisation period ends

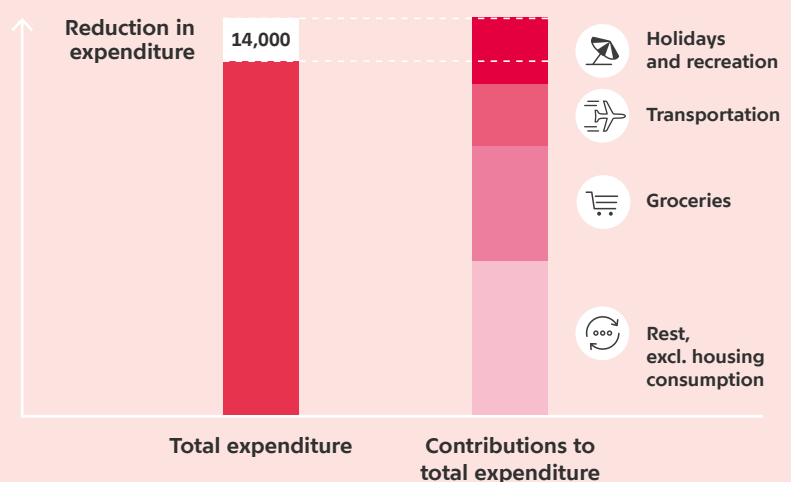
Homeowners' with interest-only mortgages reduce consumption by an average of 3 per cent of income when amortisation starts if they are unable to roll over their interest-only loans into new ones as they might have expected to do. This corresponds to a reduction in expenditure of kr. 14,000 per homeowner per year. One would expect that borrowers want their consumption ratios to vary as little as possible. Hence, the consumption reduction can be explained by the fact that a group of borrowers are unable to roll over their interest-only loans, contrary to their

expectations. This induces them to cut back consumption when amortisation begins.

Consumption drops when amortisation begins for highly leveraged, hand-to-mouth homeowners. In other words, their LTV ratios are so high that they will probably be unable to roll over their interest-only loans.

The average reduction in household expenditure of 3 per cent is significant and permanent. Homeowners

### Reduction in expenditure when non-amortisation periods end



Source: Statistics Denmark, Household Budget Survey 2017.

who cut back spending also, on average, tend to save less and increase other types of debt, e.g. bank loans or consumer loans.

These are the findings in a Working Paper prepared by Henrik Yde Andersen, Stine Ludvig Bech and Alessia De Stefani, economists at Danmarks Nationalbank.

Interest-only mortgages were introduced in Denmark in 2003 as an option for homeowners to pay interest and administration margins only to mortgage credit institutions, deferring instalments on the mortgage for up to 10 years. This is particularly an advantage for young people setting up as a family or older people with substantial home equity and a low current income.

Previous analyses in the literature have focused on how consumption patterns change when e.g. unemployment benefits expire or on retirement. The new Working Paper analyses another type of anticipated shock to the economy, namely the end of the non-amortisation period on mortgages. It investigates the effect on the finances of a large, representative subset of the population, spanning various income brackets and age groups.

At the end of the non-amortisation period, the homeowner must decide whether to apply for a

new mortgage with non-amortisation for another 10 years. Alternatively, the homeowner's budget must allow payment of instalments. If none of this happens, the homeowner has to cut back consumption.

On average, instalments after expiry increase by the equivalent of 9 per cent of household income. Consequently, homeowners who are unable to roll over their interest-only loans are forced to cut back expenditure or at least reduce other savings and begin to pay instalments. The only other option is to sell the property.

Less than one in three homeowners who have had a non-amortisation period of 10 years raise new loans with or without amortisation. Most people in the group keep the same mortgage loans even after expiry of the non-amortisation period. This may be the optimal solution for many homeowners, but a small share of the group would probably have wanted to continue with non-amortisation. There are strong indications that some of the homeowners with interest-only mortgages see them as permanent. When they turn out not to be permanent, these homeowners' daily consumption opportunities are heavily impacted.

Find the Working Paper at Danmarks Nationalbank's website ([link](#)).

## ABOUT NEWS



News are news articles based on analyses, working papers or other longer texts from Danmarks Nationalbank. News primarily

address journalists, politicians, government officials, specialists and others who want to be updated on current topics.

The news article consists of a Danish and an English version. In case of doubt regarding the correctness of the translation the Danish version is considered to be binding.

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