

DANMARKS NATIONALBANK

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Who buys the 1 per cent mortgage bond?

30-year fixed-rate mortgage bonds with coupon rate of 1 per cent has since the introduction increased to kr. 116 billion. Of this, kr. 81 billion is issued in July alone, which is the largest monthly issue to date for 30-year mortgage bonds. Homeowners have converted mortgages to lower coupon rates to a record extent, in connection with the falling market rates.

In particular, the insurance and pension sector (I&P) has been interested in the bonds and accounts for 47 per cent of the net purchases. Foreign investors have also been very interested with 31 per cent.

I&P gets the duration back, but gets lower returns

For I&P, it is important to have assets with a long maturity, and thus long duration, to match the long-term pension obligations. When homeowners convert their fixed-rate mortgages, the underlying bonds, e.g. held by I&P, are redeemed. This means that the residual maturity, and thus the duration, of the bonds will decrease, and that I&P will invest in something else than the bonds redeemed.

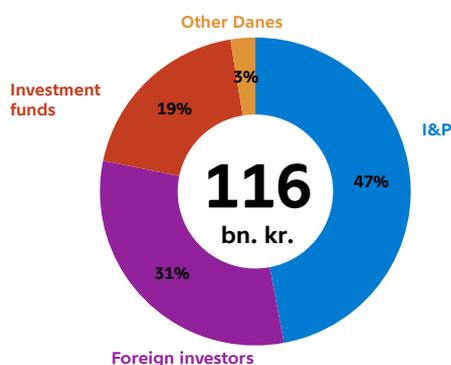
The duration of the 1 per cent coupon rate is higher than on bonds with higher coupon rates because they are less likely to be extraordinarily redeemed. The interest rate, on the other hand, is lower, which means that the Danes receive a relatively lower interest rate return on pension savings in mortgage bonds.

The bonds concern the mortgages in October

A large part of the increase in mortgage bonds is due to mortgage loan conversions, which come into effect from October 1 (The October term). Homeowners must give notice of termination of their mortgage loans at least two month before, i.e. at the end of July. In the October term, mortgage bonds were extraordinarily redeemed for a total of kr. 183 billion.¹

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I&P, foreign investors and investment funds buys bonds with a 1 per cent coupon rate



Note: Net transactions in 30-year fixed rate Danish callable mortgage with 1 per cent coupon interest issued in May-July. I&P includes underlying investment funds.

¹ If the borrower secures the new mortgage on termination of the existing loan, the mortgage institution will issue the bonds behind the new loan on a continuous basis thereafter. Investors already buy the new issues before the current term when the old bonds are replaced. If the borrower does not hedge, the mortgage bonds will be issued around the time when the new loan takes effect, for example in early October.