FINANSTILSYNET

Mortgage-credit institutions

Market Developments 2015

FINANSTILSYNET

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Market developments for mortgage-credit institutions in 2015

1. Summary

Mortgage-credit institutions improved their results considerably in 2015. Profit before tax increased from DKK 8.7 bn. in 2014 to DKK 14.6 bn. in 2015. This improvement is particularly attributable to increased net interest income, lower impairment charges, as well as improved income from associates and group undertakings.

The increased net interest income is attributable to a rise in the administration margin- and equity earnings for mortgage-credit institutions. The increase in administration margin is due to the fact that, since 2008, the financial sector as a whole has become subject to more and stricter requirements, resulting in higher costs of capital. Furthermore, the increases also reflect initiatives by the mortgage-credit sector to provide customers with an incentive to choose loan types with longer funding.

Impairments on loans from mortgage-credit institutions decreased in 2015. Thus, impairment charges are returning to the same level as before 2008. The annual impairment loss ratio of mortgage-credit institutions (impairment charges as a percentage of loans) was 0.07% in 2015.

Total mortgage-credit loans increased during the financial crisis and have been increasing since, although the increase in recent years has been rather limited. Total lending by mortgage-credit institutions increased by 0.6% in 2015.

Floating-rate loans continue to represent the majority of total lending, with 67% of lending being floating-rate in 2015. However, the percentage floating-rate loans with a fixed-interest period of up to and including one year fell. Since 2012, fixed-rate loans have made up an increasingly greater percentage of mortgage-credit institution lending. This percentage has decreased by 6 percentage points since 2012.

The share of interest-only loans has been falling since 2011, and at the end of 2015 interest-only loans made up 49% of total mortgage-credit lending, against 54% in 2011.

The development in loan types follows the intentions in the Danish FSA's supervisory diamond for mortgage-credit institutions, which, among other things, has benchmarks for non-repayment and floating-rate loans in the portfolio. The benchmarks will be launched from 1 January 2018 or 1 January 2020, respectively.[1]

The capital position of mortgage-credit institutions improved again in 2015. At the end of 2015, the total capital ratio of mortgage-credit institutions was 23.1%, against 20.8% in the previous year. However, mortgage-credit was challenged by new requirements for credit-institution capitalization.

[1] See also Market developments 2014 for mortgage-credit institutions for further description of the benchmarks in the supervisory diamond.

For several reasons, it is difficult to assess the return on equity of mortgage-credit institutions. However, for a long period, the return has been lower, yet more stable, than the return on equity of banks.

2. Main trends in the financial statements of mortgage-credit institutions

Mortgage-credit-institution earnings increased in 2015. Improvements have been particularly boosted by increased net interest income and lower impairment charges compared with the previous year.

In 2015, mortgage-credit institutions generated profits before tax of DKK 14.6 bn., see table 1. This is an increase of DKK 5.9 bn. compared with 2014, where the profit before tax was DKK 8.7 bn. Excluding income from associates and group undertakings, which is primarily attributable to one institution, mortgage-credit institutions still saw an increase in net profit for the year before tax of DKK 2.3 bn. from DKK 9.1 bn. in 2014 to DKK 11.4 bn. in 2015.[2]

Table 1: Financial statements of mortgage-credit institutions 2011-2015

						Change	
DKK mill.	*2011*	*2012*	*2013*	*2014*	*2015*	2011-2015	2014-2015
Income statement items (extract)							
Net interest income	17,353	20,273	20,974	22,375	23,686	6.4%	5.9%
Dividends from shares etc.	74	115	240	74	134	12.6%	81.1%
Net fee and commission income	-1,884	-1,636	-2,374	-2,086	-2,409	-5.0%	-15.5%
Net interest and fee income	15,543	18,752	18,839	20,363	21,412	6.6%	5.2%
Value adjustments	-2,761	-952	-620	-746	-1,132	16.3%	-51.7%
Staff and administrative expenses	5,131	4,860	5,008	4,780	4,828	-1.2%	1.0%
Impairments on loans etc.	2,841	3,922	4,811	4,707	1,868	-8.0%	-60.3%
Income from associates and group undertakings	650	668	685	-374	3,195	37.5%	*
Profit before tax	4,812	9,002	8,190	8,713	14,591	24.8%	67.5%
Tax	884	1,998	1,758	2,336	3,098	28.5%	32.6%
Net profit for the year	3,929	7,004	6,433	6,378	11,493	23.9%	80.2%
Balance sheet items (extract)							
Due from credit institutions	623,011	677,770	714,365	781,905	731,966	3.3%	-6.4%
Lending	2,501,477	2,587,598	2,589,292	2,636,353	2,652,662	1.2%	0.6%
Bonds	188,376	177,186	195,020	234,826	199,649	1.2%	-15.0%
Shares etc.	4,265	4,120	3,831	4,379	5,021	3.3%	14.7%
Debt to credit institutions	663,536	660,380	669,549	698,974	665,453	0.1%	-4.8%
Issued bonds	2,473,733	2,609,150	2,664,798	2,782,031	2,749,817	2.1%	-1.2%
Subordinated debt	23,954	19,392	16,914	15,205	12,907	-11.6%	-15.1%
Equity	150,429	158,140	162,521	168,931	180,804	3.7%	7.0%
Balance sheet total	3,387,676	3,512,976	3,565,792	3,717,482	3,647,170	1.5%	-1.9%

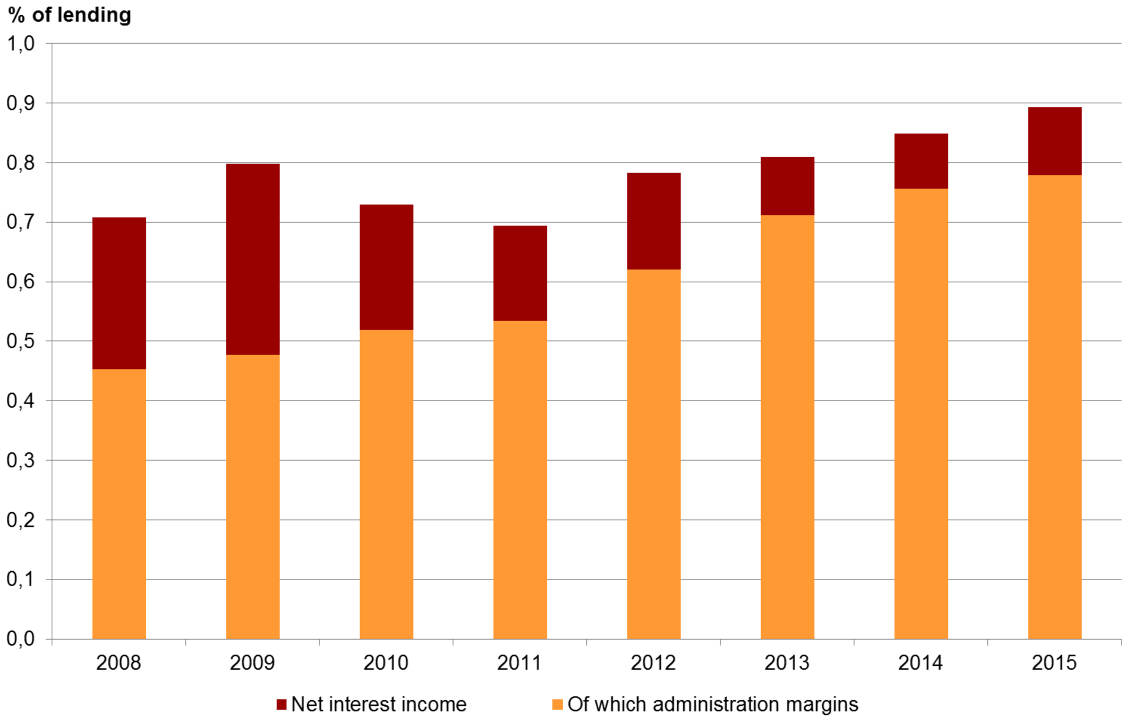
Note: In 2015, the mortgage-credit sector comprised Nykredit Realkredit, Realkredit Danmark, Totalkredit, BRFkredit, DLR Kredit, LR Realkredit and Nordea Kredit. The profit from equity investments and equity for Totalkredit is included

[2] Excluding amortisation/depreciation and impairment charges by Nykredit Realkredit on intangible assets and property, plant and equipment, the profit before tax of the sector was DKK 13.5 bn. in 2015, against DKK 10.1 bn. in 2014, corresponding to an increase of DKK 3.4 bn.

twice, as it is part of the Nykredit group. The income from associates and group undertakings is mainly attributable to subsidiary companies in Nykredit Realkredit: Totalkredit and Nykredit Bank. Subsidiary companies are included with their net earnings. This means that the part of the results attributable to Totalkredit includes the administration margin and expenses paid to banks in connection with management and administration of the mortgage-credit institution. Net profits for Nykredit Bank are also influenced by mortgage-credit activities and customer relations in these, e.g. value adjustments of interest-rate swaps taken up to hedge the interest-rate risk of customers. The consolidated mortgage-credit result (DKK 11.5 bn. after tax for the sector in total) is the same as the result and net earnings at individual institution level shown in table 1, as in this case the net earnings of subsidiary undertakings are recognized in the income from associates and group undertakings.
Source: Reports to the Danish FSA.

The net interest income of mortgage-credit institutions rose from DKK 22.4 bn. in 2014 to DKK 23.7 bn. in 2015, corresponding to an increase of 6.4%. In relation to lending, total net interest income was 0.89% in 2015, which is slightly higher than the 2014 figure of 0.85%, see figure 1.

Figure 1: Development in net interest income and administration margins, 2008-2015



Source: Reports to the Danish FSA.

The increase in net interest income in recent years is attributable to increased administration margins and higher earnings on investment portfolios. In 2015, the administration margins of mortgage-credit institutions came to DKK 20.7 bn. against DKK 19.9 bn. in the previous year, corresponding to an increase of 3.6%. As a percentage of lending, the administration margins came to 0.78% in 2015 against 0.76% in 2014. In 2015, income on investment portfolios increased slightly from 2014 due to increasing business, e.g. more conversion activity. Since 2008, the percentage of lending represented by administration margins has been increasing, whereas the percentage of total net interest income from the investment portfolio has been falling; among other things due to low interest-rate levels.

Mortgage-credit institutions pay net commissions, as customers often take out mortgage-credit loans through banks, and these carry out much of the administration for mortgage-credit institutions. In 2015, mortgage-credit institutions paid net fees of DKK 2.4 bn. against DKK 2.1 bn. in 2014.

Overall, net interest and fee and commission income came to DKK 21.4 bn. in 2015 against DKK 20.2 bn. in 2014, corresponding to an increase of 5.8%.

The income from associates and group undertakings (subsidiary companies and sharehold-ings) contributed positively with DKK 3.2 bn. in 2015 against a negative result of DKK 0.4 bn. in 2014. The positive result derives particularly from one institution in which the results on income from associates and group undertakings contributed positively (see the note in table 1 and appendix 2).

In 2015, value adjustments constituted a loss of DKK 1.1 bn. against a loss of DKK 0.7 bn. in the previous year. The deterioration is attributable to losses on currency and interest-rate contracts as well as losses on the bonds portfolios.

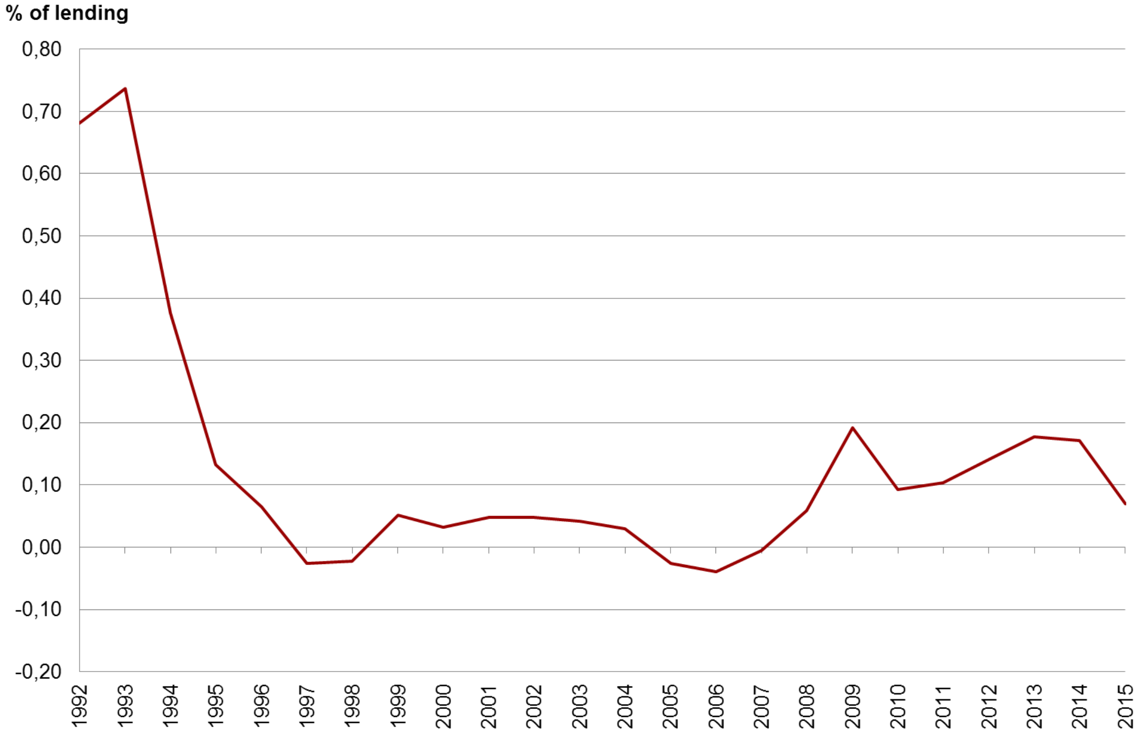
Lending by mortgage-credit institutions accounted for DKK 2,653 bn. in 2015 against DKK 2,636 bn. in 2014, which is an increase of 0.6%. Loans for owner-occupied residences and recreational properties came to 56.4% whilst corporate segments came to 43.6%.

Impairment charges

Impairments on loans by mortgage-credit institutions came to DKK 1.9 bn. in 2015, which is a decrease of DKK 2.8 bn. compared with 2014, when impairments on loans were DKK 4.7 bn. The lower impairments on loans are thus a significant reason for the improvements in mortgage-credit institutions' results for the year. The annual impairment loss ratio (annual impairment losses charged as a % of lending) was 0.07% in 2015 and thus fell by 0.10 per-centage points compared with the previous year, see figure 2. This is the lowest level since 2008. The increase should be seen in light of lower interest rates and increasing housing prices.

Historically, the impairment loss ratio of mortgage-credit institutions has been low, and for comparison, the annual impairment loss ratio was around 0.7% in the early 1990s.

Figure 2: Annual impairment loss ratio of mortgage-credit institutions, 1992-2015

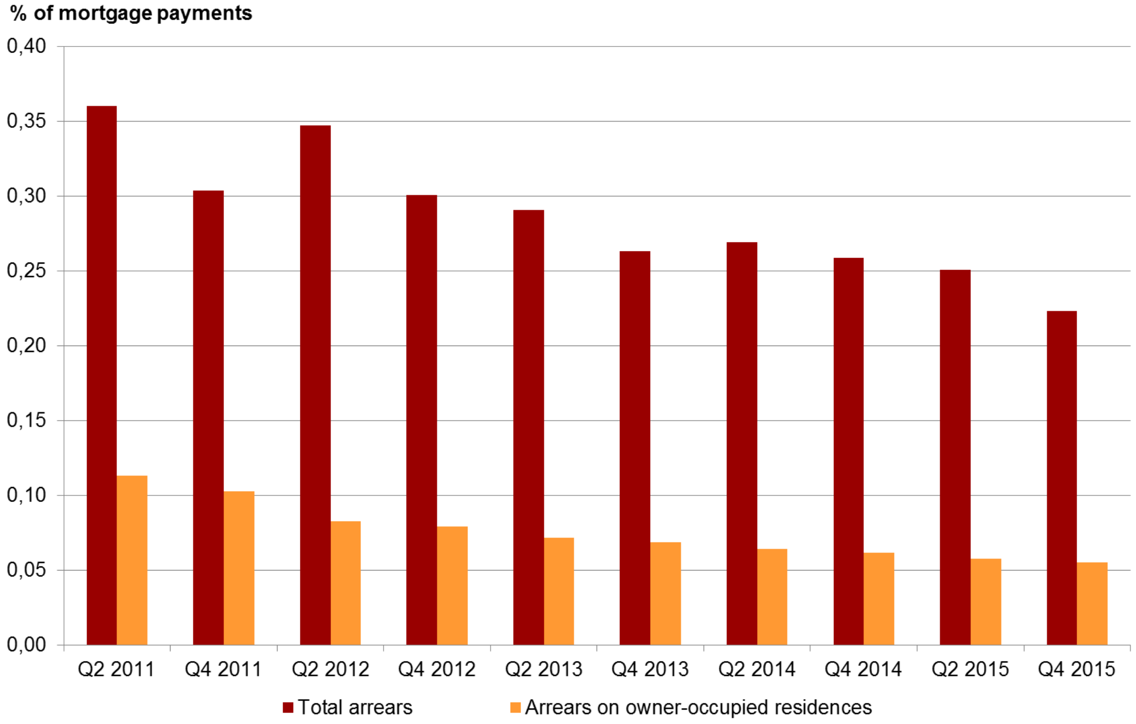


Source: Annual reports and reports to the Danish FSA

Arrears

The extent of arrears (i.e. repayments not paid in due time) was 0.22% of the all mortgage payments in Q4 2015 and has thus fallen compared with 0.26% at the same time last year, see figure 3. Since Q2 2012, total arrears as a percentage of mortgage payments has been falling. The same has been the case for arrears on owner-occupied residences. At the end of 2015, arrears on owner-occupied residences were 0.05% of mortgage payments.

Figure 3: Developments in arrears due to mortgage-credit institutions in relation to mortgage payments, 2011-2015



Note: Arrears are calculated as the sum of arrears after 3½ months, 6½ months and 12½ months.
Source: Reports to the Danish FSA.

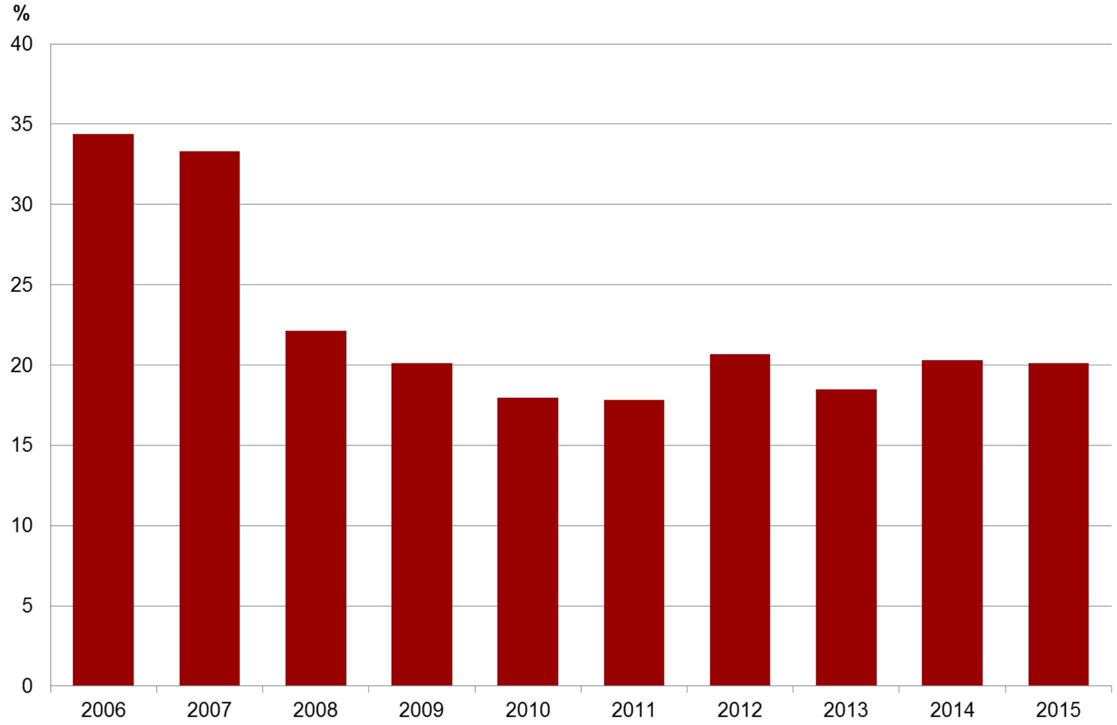
Coverage ratio

Coverage ratio is a measurement of the size of impairment losses on bad loans. The financial ratio is calculated as total accumulated impairment losses (on individually assessed loans) in relation to the part of the loan portfolio which has been subject to impairment. The larger the coverage ratio, the greater the coverage in the form of impairment on the bad loans.

At the end of 2015, mortgage-credit institutions had a coverage ratio of 20.1% against 20.3% at the end of 2014, see figure 4. For comparison, the coverage ratio for banks was 50.3% at the end of 2015.

All else being equal, the coverage ratio should be lower for mortgage-credit institutions than for banks because of the collateralization behind mortgage-credit loans.

Figure 4: Coverage ratio for mortgage-credit institutions, 2006-2015



Source: Reports to the Danish FSA.

Selected financial ratios

The capital ratio of mortgage-credit institutions was 23.1% in 2015, see table 2. This is an increase of 2.3 percentage points compared with end-2014. Moreover, the Tier 1 capital ratio increased from 20% to 21.5%, whereas the Common Equity Tier 1 capital ratio increased from 19.1% at the end of 2014 to 20.9% at the end of 2015.

Note that own funds increased by a greater percentage than lending in the period 2011-2015, and that the total risk exposure fell in the same period (see also appendix 3). The fall in total risk exposure should be viewed in light of the fact that the underlying factors triggering risk exposures have improved. Rising housing prices and falling LTV have reduced risk-weights.

The ratio of operating income to operating expenses for mortgage-credit institutions (i.e. total DKK earned for each DKK spent) increased from DKK 1.81 at the end of 2014 to DKK 2.62 at the end of 2015.

Table 2: Selected financial ratios 2011-2015

%	***2011***	***2012***	***2013***	***2014***	***2015***
Ratio of operating income to operating expenses (DKK)	1.55	1.94	1.76	1.81	2.62
Return on equity before tax	3.25	5.84	5.09	5.21	8.35
Total capital ratio	18.87	19.36	19.55	20.8	23.09
Tier 1 capital ratio	18.52	18.92	19.13	19.98	21.47
Common Equity Tier 1 capital ratio	16.64	17.75	18.34	19.06	20.92

Source: Reports to the Danish FSA.

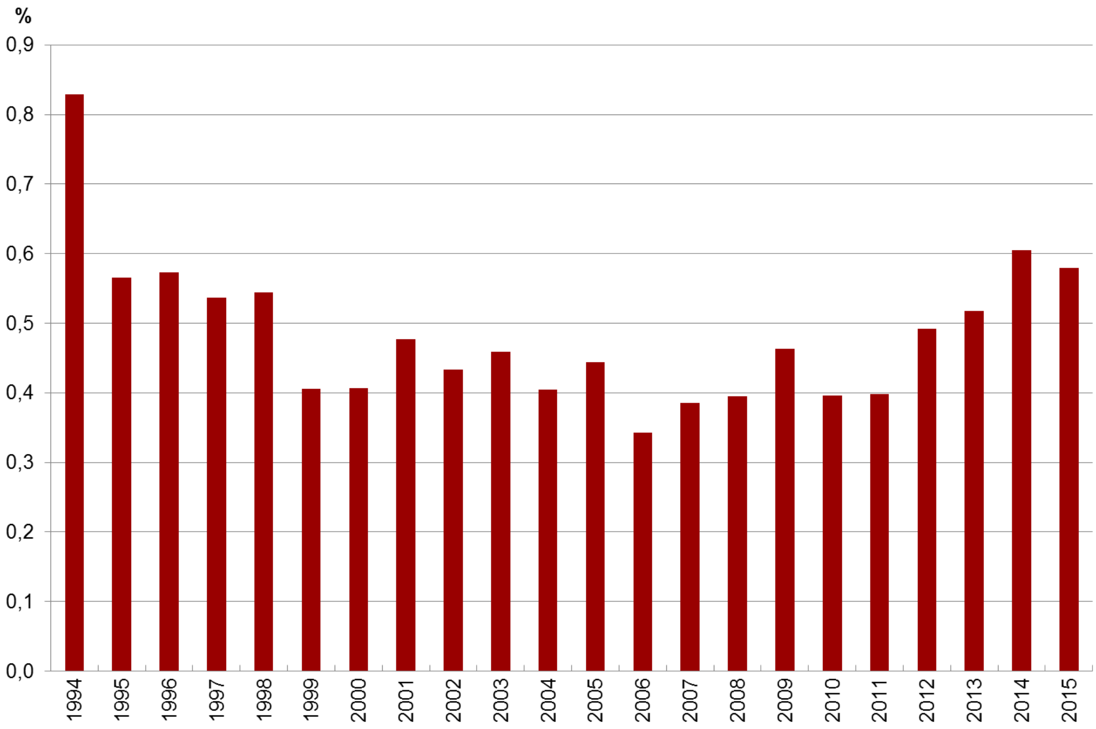
Core earnings

Core earnings are profits/losses before impairment losses, market value adjustments, and profits/losses on participating interests. Core earnings should be able to cover the expected losses on lending activities such that only large unexpected losses need to be absorbed by equity. Core earnings must also pay interest on equity.

Compared with banks, mortgage-credit institutions are generally characterized by having lower core earnings in relation to lending. This is partly due to the fact that impairment losses in mortgage-credit institutions have been lower historically than the impairment losses of banks. Over the past 20 years, impairment charges by mortgage-credit institutions have on average been at 0.06% of total lending, against 0.6% for banks in the same period.

Figure 5 shows a simple average of the core earnings of mortgage-credit institutions since 1994, measured in relation to lending. In 2015, core earnings in relation to lending came to 0.58%, which is basically at par with the 0.6% in the previous year. Thus, in light of the historical losses, mortgage-credit institutions have a significant first buffer to counter credit losses.

Figure 5: Core earnings in relation to lending, 1994-2015



Note: Core earnings contain all income-statement items except impairments on loans, market value adjustments and profits/losses on participating interests. In the 1990s, LR Realkredit had very high core earnings in relation to lending and is not included in the average.

Source: Reports to the Danish FSA.

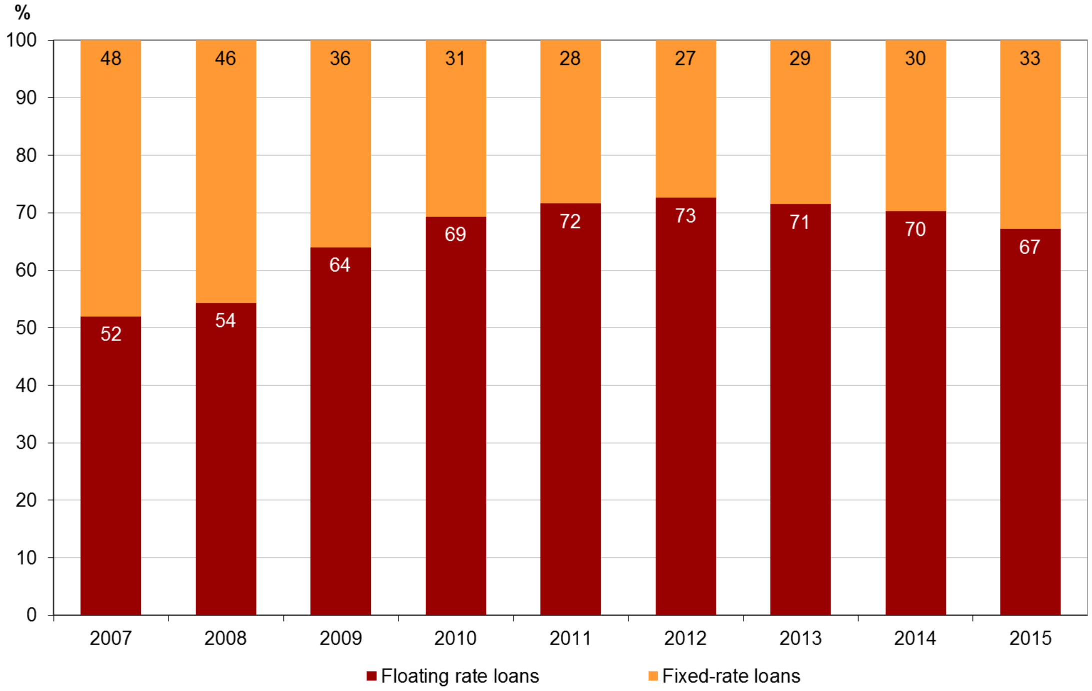
3. Loan types

In recent years, the percentage of floating-rate loans and interest-only loans in the total lending by mortgage-credit institutions has been falling, though from a very high level. Similarly, the percentage of floating-rate loans with a very short fixed-interest period has fallen.

Floating-rate loans

Since 2007, floating-rate loans have made up the majority of mortgage-credit institution lending, and in 2015 floating-rate loans accounted for 67%, see figure 6. The percentage of fixed-rate loans in total lending has been increasing slowly since 2012, and this trend continued in 2015, when fixed-rate loans made up 33% of total lending; an increase of 3 percentage points compared with the same time in the previous year.

Figure 6: Floating-rate lending and fixed-rate lending by mortgage-credit institutions as a percentage of total lending, 2007-2015



Note: Floating-rate lending includes variable-interest loans linked to a referenced interest rate (CITA/CIBOR), and variable-interest loans with an interest ceiling (not reached).

Source: Danmarks Nationalbank, MFI statistics.

At the end of 2015, lending with a fixed-interest period of more than 1 year made up 42.3% of variable-interest loans, see figure 3. This percentage has been increasing since 2008, when it was 23.5%. Floating-rate loans with a fixed-interest period of up to and including 1 year made up 57.7% at the end of 2015 and continue to make up the greatest percentage of variable-interest loans.

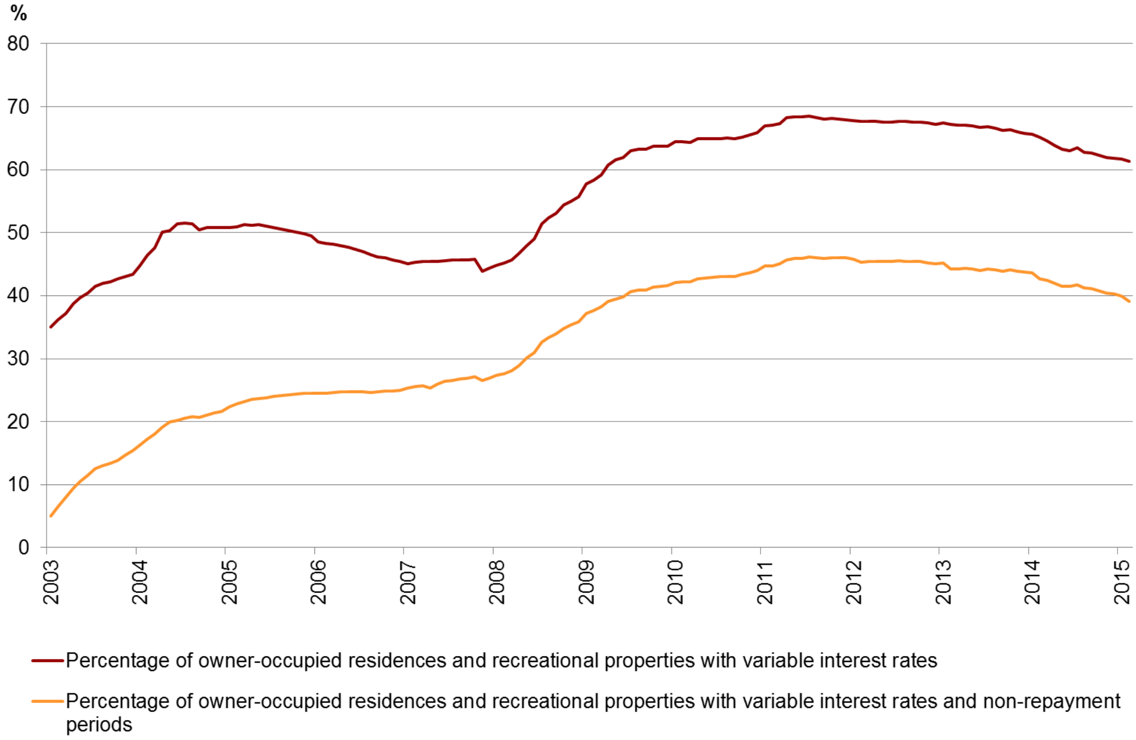
Table 3: Lending with a fixed-interest period of up to and including 1 year and more than 1 year, respectively, in relation to the portfolio of variable-interest loans, 2004-2015

%	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Maturity up to and including 1 year	57.9	72.1	75.7	76.2	76.5	75.8	73.1	71.7	69.9	65.4	62.8	57.7
Maturity more than 1 year	42.1	27.9	24.3	23.8	23.5	24.2	26.9	28.3	30.1	34.6	37.2	42.3

Note: Variable-interest loans are ordinary floating-rate loans as well as variable loans with an interest ceiling.
Source: Reports to the Danish FSA

Floating-rate loans and other variable-interest loans for owner-occupied residences and recreational properties made up about 62% of total lending for owner-occupied residences and recreational properties at end-2015, see figure 7. Out of the total variable-interest loans for owner-occupied residences and recreational properties, about 65% of the loans had a non-repayment (interest only) period. The percentage of loans for owner-occupied residences and recreational properties with variable interest and non-repayment thus came to about 40% of total loans for owner-occupied residences and recreational properties at end-2015.

Figure 7: Percentage of variable fixed-interest loans and interest-only variable-interest loans for owner-occupied residences and recreational properties in relation to total lending by mortgage-credit institutions for owner-occupied residences and recreational properties, 2003-2015

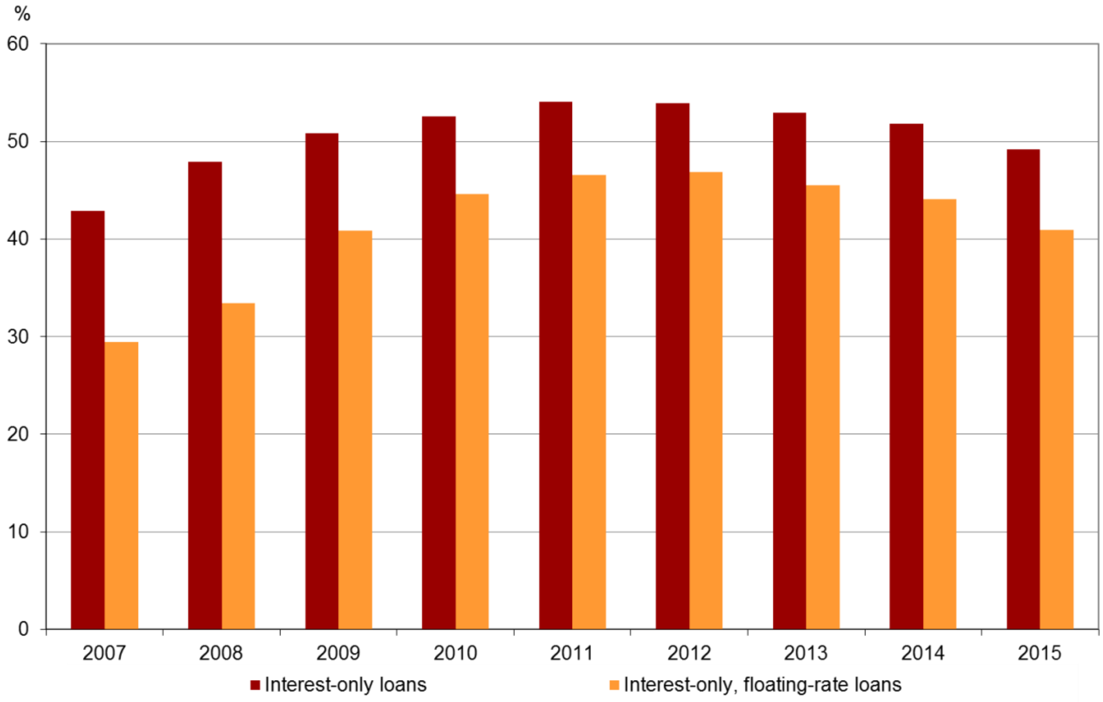


Source: Danmarks Nationalbank, MFI statistics.

Non-repayment

Since 2011, the percentage of interest-only loans out of the total mortgage-credit loans has been falling slightly. At the end of 2015, interest-only loans amounted to 49% of total mortgage-credit lending, and this is a drop of about 3 percentage points compared with the same time in the previous year, see figure 8. In the same period, the percentage of interest-only floating-rate loans out of total lending has also fallen.

Figure 8: Percentage of interest-only loans and interest-only, floating-rate loans in relation to total lending by mortgage-credit institutions, 2007-2015



Source: Danmarks Nationalbank, MFI statistics

4. Trends in administration margins

Since 2008, the administration margins of mortgage-credit institutions have generally been increasing. The increase has been most profound on more risky loan products such as floating-rate loans with a very short fixed-interest period, as well as interest-only loans. Among other things, this is a consequence of efforts by mortgage-credit institutions to influence the incentive of customers to choose fewer loan products of this type. This trend is in line with the benchmarks in the Danish FSA's supervisory diamond for mortgage-credit institutions, which will be implemented with effect from 1 January 2018 and 1 January 2020, respectively.

The administration margins are the primary source of income for mortgage-credit institutions. Together with possible extra brokerage fees and other fees, the administration margin is the payment from debtor to the mortgage-credit institution for costs of capital, managing the loan, and hedging the credit risk. For corporate customers, the administration margin is generally negotiated individually with the institution, whereas for private customers, traditionally, there is fixed pricing for all customers, depending on loan type and loan-to-value etc. (see also box 1).

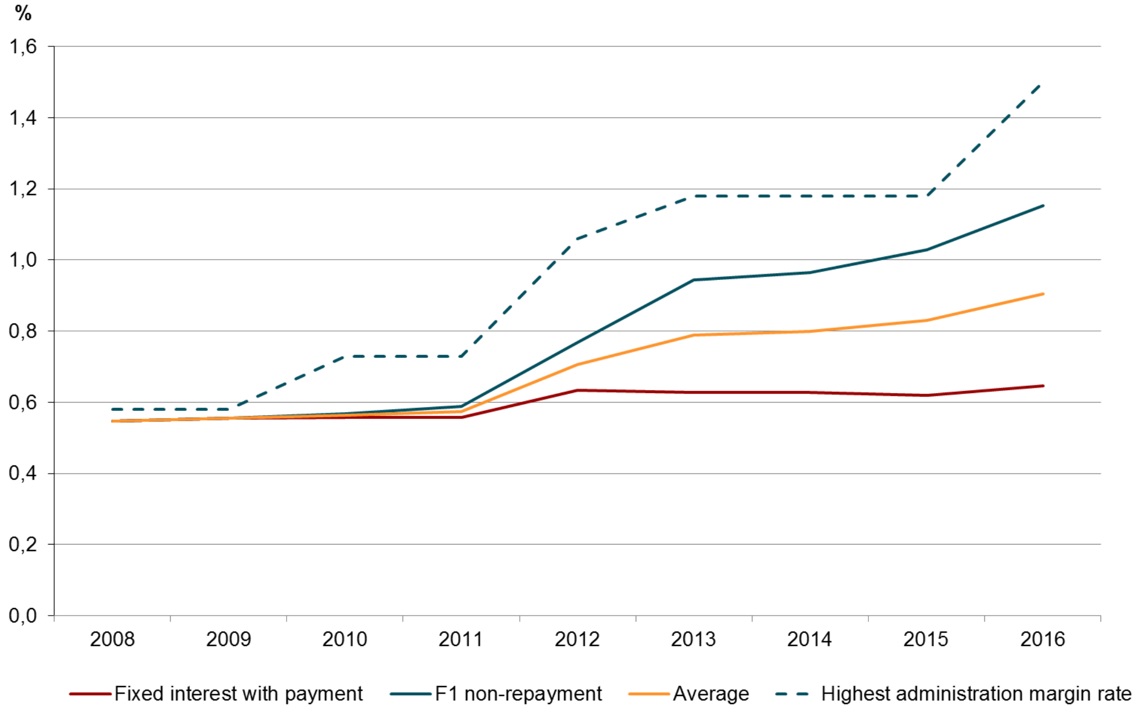
Box 1: Rules for increases in the administration margin

The option of mortgage-credit institutions to raise the administration margin is regulated by the rules on good business practices in financial undertakings, which are for consumer protection in the financial sector. The good business practice regulations were tightened on 1 November 2015.

Pursuant to the rules, the administration margin cannot be increased arbitrarily, and certain conditions must be met before they are raised. First, an administration margin increase must be notified individually to the customers affected, no less than three months before the increase. Secondly, specific reasons for the administration margin increase must be given. However, price increases may be justified as merely to increase earnings.

Historically, administration margins have both increased and fallen. Since 2008, administration margins for private individuals have generally increased, see figure 9.

Figure 9: Developments in administration margins on mortgage-credit loans for private individuals mortgaging of 80% of their property value, 2008 - first half year of 2016



Note: For 2016, in Totalkredit and Realkredit Danmark this involves the announced administration margins applicable from 1 July 2016 and 1 October 2016, respectively. For all other institutions, the 2015 administration margin is carried over to 2016.
Source: Information from the mortgage-credit institutions.

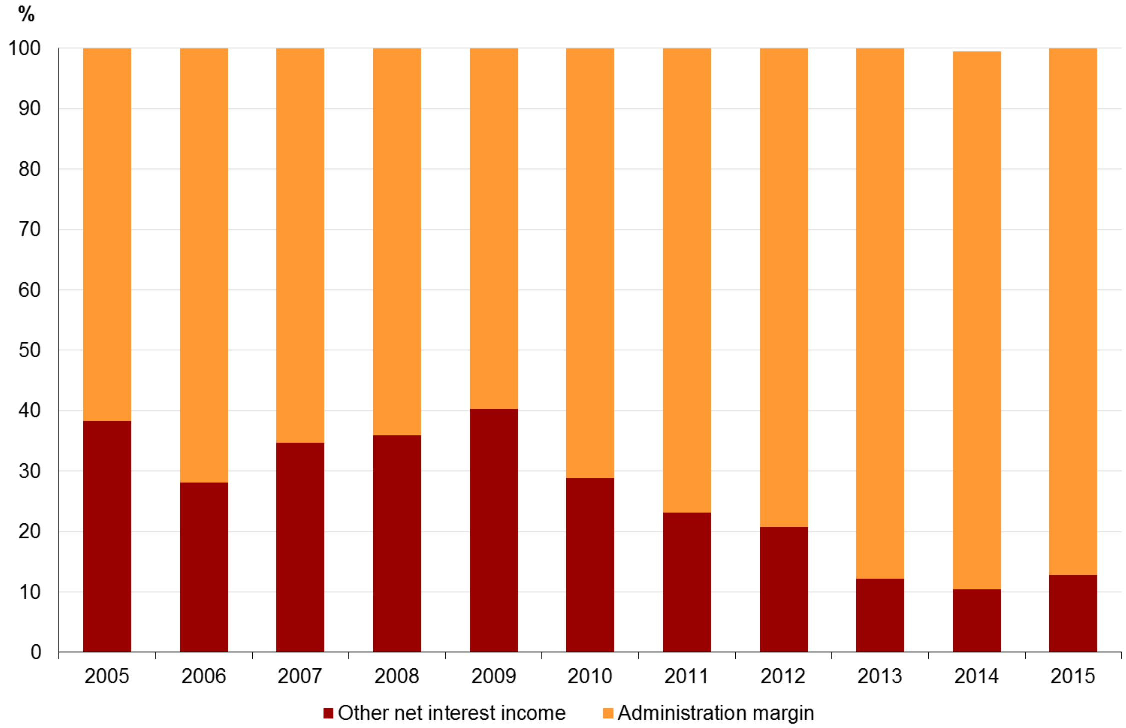
Much of the increase is attributable to initiatives by mortgage-credit institutions to give customers an incentive to change to less risky product types, as the increase is greatest on more risky products such as variable-interest loans and interest-only loans. If this is successful and customers move to less risky products, all else being equal, this may mean a fall in the total administration margin. This will be the case if the income increase on more expensive loans is lower than the income loss after customers change from expensive loans to cheaper loans.

Developments in the administration margins for different loan types follow the intention in the Danish FSA's supervisory diamond for mortgage-credit institutions, which, among other things, limits non-repayment and floating-rate loans in the portfolio.

Investment returns have had great significance for developments in mortgage-credit institution results

Previously, returns for mortgage-credit institutions on their investment portfolio made up a large percentage of total net interest income. The changed composition of the net interest income of the mortgage-credit sector is illustrated in figure 10.

Figure 10: Administration margins of mortgage-credit institutions and other net interest income as % of total net interest income, 2005-2015



Source: Reports to the Danish FSA.

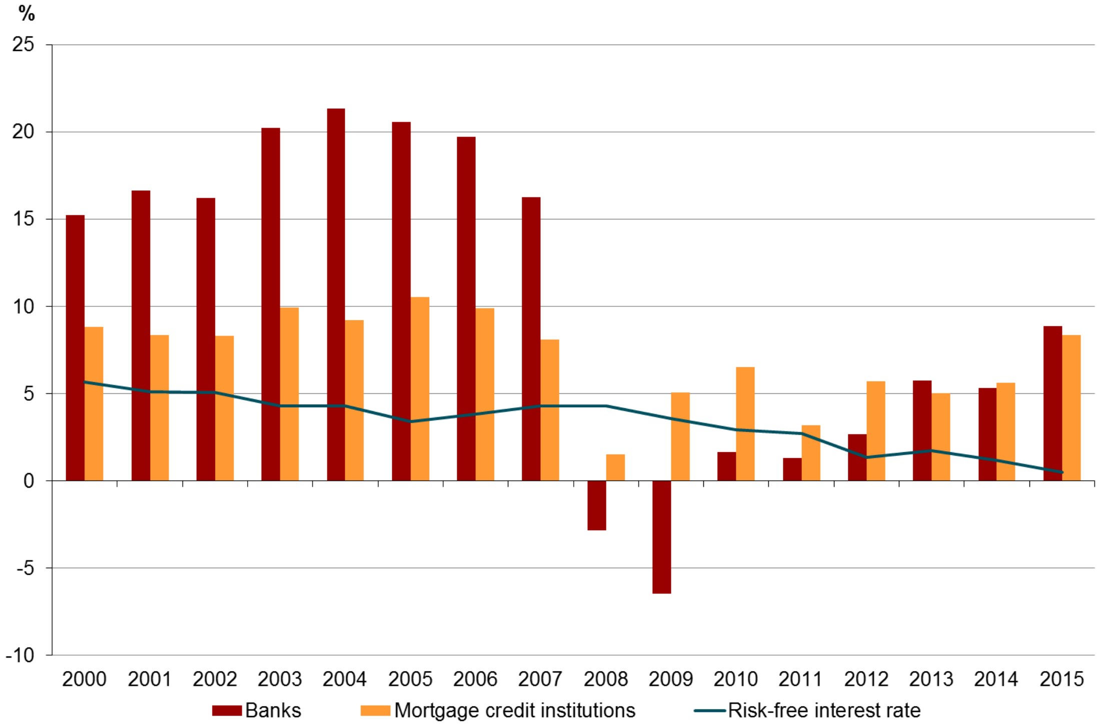
The percentage of income from lending activities (the administration margins) increased from 2005 to 2015, whereas income from e.g. placement of equity (other net interest income) has fallen. This change should be seen in light of the low interest rates in recent years.

5. Return on equity for mortgage-credit institutions

Historically, the mortgage-credit sector has had a lower return on equity than banks and fluctuations over time have been lower than in the banking sector, see figure 11. To a certain degree, this also seems natural given the more limited risk profile of mortgage-credit activity compared with banking activities. Figure 11, also shows the yield on ten-year government bonds (risk-free interest rate). The owners of mortgage-credit institutions and banks are typically remunerated with a return that reflects the underlying risk of the business activity. The risk premium in addition to the risk-free return is therefore greater for banks than for mortgage-credit institutions.

The differences in the business models of the institutions also means that it is important to be cautious when analyzing the returns for the sector and when comparing institutions. In institutions with a bank as a parent undertaking, part of the joint expenses are incurred by the parent undertaking. The genuine return on equity must thus be assumed to be lower than shown in figure 11.

Figure 11: Return on equity before tax for mortgage-credit institutions and banks, 2000-2015



Source: Reports to the Danish FSA and Danmarks Nationalbank (Central Bank of Denmark).

6. Supplementary collateral

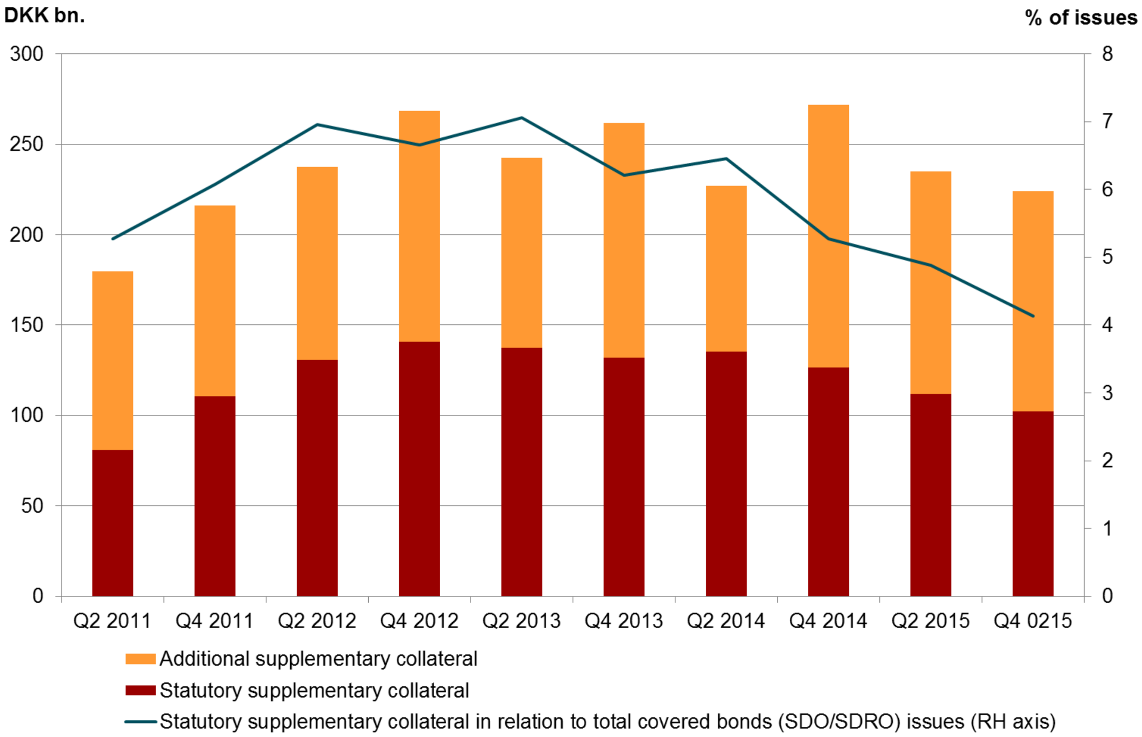
In 2007, mortgage-credit institutions were able to finance their loans with the covered bonds (SDOs/SDROs). For investors, these bonds are more secure than traditional mortgage-credit bonds and are therefore weighted less in investors' total risk exposure. Conversely, mortgage-credit institutions issuing SDOs/SDROs must put up supplementary collateral for drops in property prices which mean that lending limits are exceeded.

In Q4 2015, supplementary collateral was at DKK 224 bn., which is a drop of DKK 48 bn. compared with the previous year, when supplementary collateral made up DKK 272 bn., see figure 12.

At the end of 2015, as a consequence of exceeding lending limits on loans financed by mortgage-credit institutions with SDOs/SDROs, statutory supplementary collateral was established of just over DKK 102 bn. This corresponds to 4.1% of total issuances. Statutory supplementary collateral for owner-occupied residences amounts to 47% of statutory collateral.

In addition to the statutory supplementary collateral, mortgage-credit institutions put up additional supplementary collateral of DKK 122 bn. in Q4 2015 in order to obtain satisfactory investor assessments of the bonds.

Figure 12: Total supplementary collateral for SDO/SDRO issues, 2011-2015



Source: Reports to the Danish FSA.

7. Capitalization and capital buffers

In adopting the CRD IV, new initiatives (combined buffer requirement) were implemented on the capital side for credit institutions, including mortgage-credit institutions. The requirements include stricter requirements on both the quality of institutions' capital and on their total own funds. A simple projection of the capital requirements after phasing-in shows that mortgage-credit institutions will maintain a good level and are already in place in relation to the requirements. Future updates of the capital regulations based on new initiatives from the Basel Committee are expected to increase capital requirements considerably, however.

The transition to CRR tightened the requirements for the capital used to meet the capital requirement of 8% of the total risk exposure. Today, a minimum of 4.5% of the total risk exposures have to be met with Common Equity Tier 1 capital. Up to 2014, the corresponding requirement was 2% of the total risk exposure.

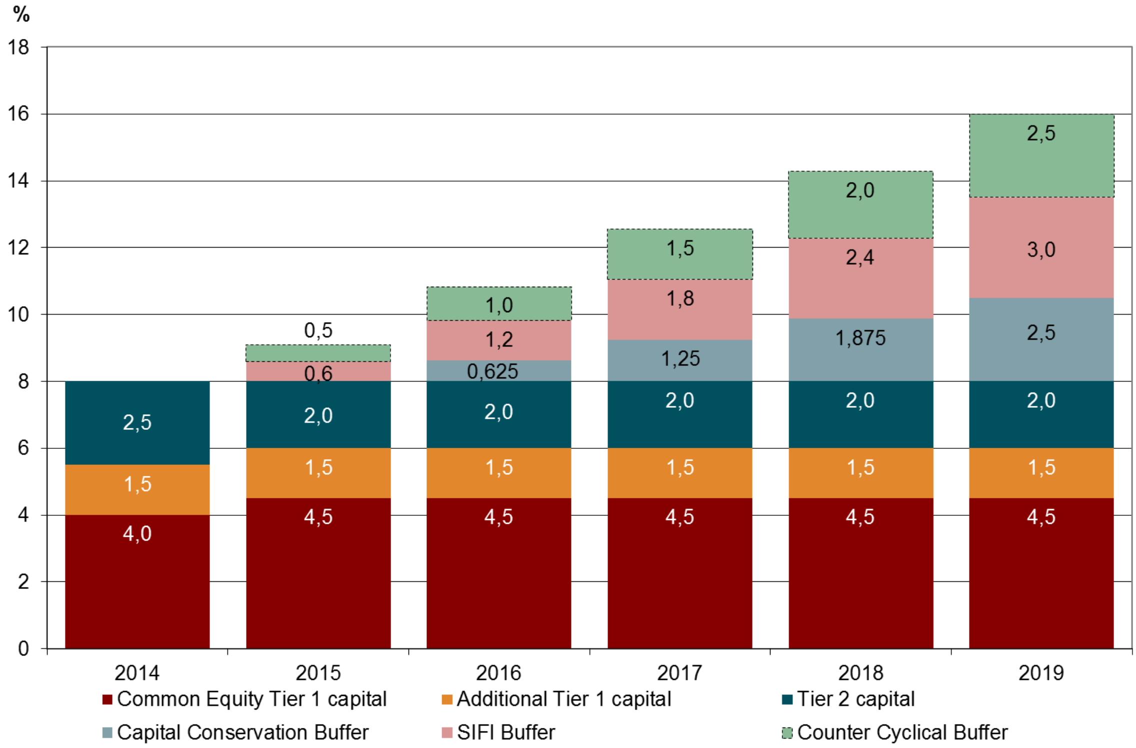
Implementation of CRD IV will introduce three capital buffers and these will be fully implemented in 2019, see figure 13. These are the capital conservation buffer, the countercyclical buffer and a systemic buffer.

The size of the systemic buffer depends on the degree of the systemic importance of the individual institution. In 2019, the systemic buffer will be between 1% and 3% of the total risk exposure, depending on systemicness. In 2019, the capital conservation buffer will make up 2.5% of the total risk exposure. The countercyclical buffer is currently set at zero, but it may be activated by the Minister for Business and Growth if required, e.g. in connection with risky growth in credit provisions.

The buffer requirements phased in gradually up to 2019 must be met with Common Equity Tier 1 capital. The combined buffer requirements introduced in Danish legislation on implementation of the CRD IV entail an increase in the capital requirement of mortgage-credit institutions. The buffer requirements affect both the current portfolios of the institutions and their future lending. This means that, the capital requirement per risk-weighted DKK of lending will increase up to 2019.

The phase-in is shown in the graph below:

Figure 13: Minimum capital requirements and phase-in of capital buffers after CRR and CRD4

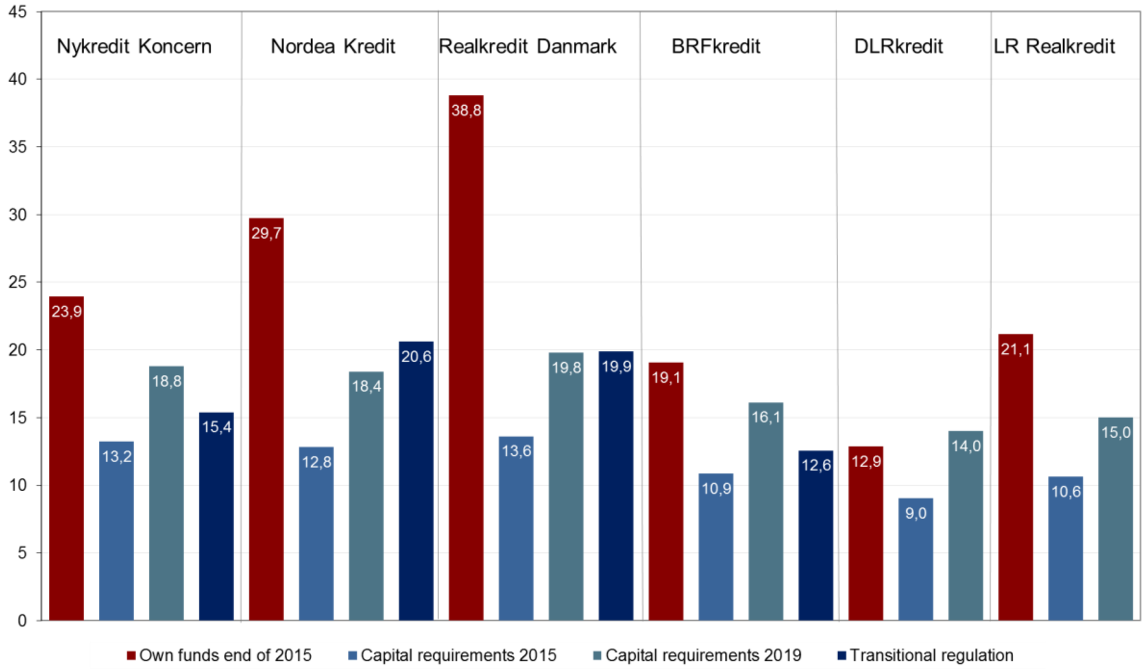


Note: The Pillar II requirement has not been included as it is measured individually for each institution.

Source: The Danish FSA.

Figure 14 shows how the own funds of individual institutions compare with a simple projection of their capital requirements for 2019. For IRB institutions, their Basel 1 floor requirements are also shown. At the end of 2015, DLR Kredit and LR Kredit were using the standard method. Accordingly, they were not subject to a Basel 1 floor requirement.

Figure 14: Capital ratios and capital requirements (gradually and fully phased-in) as well as transitional regulations (Basel 1 floor requirement), % of total risk exposure



Note: Capital requirements include minimum capital requirements (Pillar I), Pillar II requirements as well as capital conservation buffer, SIFI buffer and countercyclical buffer. LR has not been designated as a SIFI and thus is not subject to a SIFI buffer. From the end of Q1 2016, DLR became subject to the IRB method.
Source: Reports to the Danish FSA.

The projection assumes an unchanged level for the risk-weighted items. In addition, own funds are assumed to remain unchanged. The institutions may have shareholdings which up to 2019 it will not be possible to include in own funds. Thus, it is implicitly assumed that such capital will be replaced.

All else being equal, deterioration in the credit quality of the portfolio will also increase the risk-weighted items and thus the capital requirements. Similarly, deterioration in the credit quality will increase the need for a Pillar II supplement and thus lead to further increases in the capital requirement.

Lending growth expected in the sector will increase the volume of shares subject to risk-weighting, and thus the capital requirements in absolute figures.

DLR started using the IRB method for parts of its credit exposure at the end of Q1 2016; this will improve its capital situation.

The above only takes into account the future requirements known at this time.

Moreover, the European Commission is working on an expected update of the CRR/CRD IV, and the Basel Committee has also come up with new initiatives which are likely to increase the capital requirements significantly.

The new requirements of the Basel committee comprise a so-called output floor, which is to replace the existing Basel 1 floor requirement. The precise design of the output floor is not yet known, but the floor will be based on an updated version of the standard method. Depending on the final presentation, the output floor may potentially lead to an increase in the capital requirements of mortgage-credit institutions. At the same time, this will minimize the risk sensitivity of the capital requirement.

Another of the Basel Committee's new requirements concerns parameter floors that determine lower limits for the risk parameters estimated by IRB institutions themselves. In this context, the lower limits for Loss Given Default, LGD, may potentially become significant for Danish mortgage-credit institutions using the IRB method. For the most secure loans (with the lowest LTV), the loss history of institutions will thus have lower LGD values than the floors proposed by the Basel Committee. In terms of risk, this is disproportionate.

The proposals from the Basel Committee are currently subject to public consultation and may thus change before the final regulations are finalized. After this, there will be a process with implementation in the EU which may also be significant for the effect of the new regulations on Danish mortgage-credit institutions.

8. About the statistics

This article on market developments has been based on financial statements etc. submitted for mortgage-credit institutions in Denmark. Figures are at institution level, unless otherwise stated.

This article focuses on developments in selected accounts items and financial ratios at sector level and on the underlying developments in the individual mortgage-credit institutions. At a later stage, the Danish FSA will publish "Statistical data for mortgage-credit institutions". This publication will contain more data from mortgage-credit institutions' submissions for 2015. Moreover an update will follow of financial ratios in the five-year financial summary, analyzed by the individual institutions in the financial ratios database on the Danish FSA website.

All mortgage-credit institutions are covered by the statistics.

9. Appendices

Appendix 1: Financial statements of mortgage-credit institutions 2011-2015

						Change	
DKK mill.	*2011*	*2012*	*2013*	*2014*	*2015*	*2011-2015*	*2014-2015*
Income statement items (extract)							
Net interest income	17,353	20,273	20,974	22,375	23,686	6.4%	5.9%
Dividends from shares etc.	74	115	240	74	134	12.6%	81.1%
Net fee and commission income	-1,884	-1,636	-2,374	-2,086	-2,409	-5.0%	-15.5%
Net interest and fee income	15,543	18,752	18,839	20,363	21,412	6.6%	5.2%
Value adjustments	-2,761	-952	-620	-746	-1,132	16.3%	-51.7%
Staff and administrative expenses	5,131	4,860	5,008	4,780	4,828	-1.2%	1.0%
Impairments on loans etc.	2,841	3,922	4,811	4,707	1,868	-8.0%	-60.3%
Income from associates and group undertakings	650	668	685	-374	3,195	37.5%	*
Profit before tax	4,812	9,002	8,190	8,713	14,591	24.8%	67.5%
Tax	884	1,998	1,758	2,336	3,098	28.5%	32.6%
Net profit for the year	3,929	7,004	6,433	6,378	11,493	23.9%	80.2%
Balance sheet items (extract)							
Due from credit institutions	623,011	677,770	714,365	781,905	731,966	3.3%	-6.4%
Lending	2,501,477	2,587,598	2,589,292	2,636,353	2,652,662	1.2%	0.6%
Bonds	188,376	177,186	195,020	234,826	199,649	1.2%	-15.0%
Shares etc.	4,265	4,120	3,831	4,379	5,021	3.3%	14.7%
Holdings in associated undertakings	29,998	31,363	32,146	31,562	36,251	3.9%	14.9%
Assets held temporarily	1,835	1,337	1,005	880	1,070	-10.2%	21.6%
Other assets	27,130	25,066	22,227	22,739	17,154	-8.8%	-24.6%
Total assets	3,387,676	3,512,976	3,565,792	3,717,482	3,647,170	1.5%	-1.9%
Debt to credit institutions	663,536	660,380	669,549	698,974	665,453	0.1%	-4.8%
Issued bonds	2,473,733	2,609,150	2,664,798	2,782,031	2,749,817	2.1%	-1.2%
Other non-deriv. finan. liabs. at fair value	4,421	2,025	862	1,188	427	-37.3%	-64.1%
Current tax liabilities	228	43	25	169	99	-15.4%	-41.4%
Other liabilities	67,536	60,375	50,218	50,204	37,013	-11.3%	-26.3%
Total debt	3,211,921	3,334,387	3,385,481	3,532,623	3,452,839	1.5%	-2.3%
Total provisions	1,371	1,057	876	723	620	-14.7%	-14.2%
Subordinated debt	23,954	19,392	16,914	15,205	12,907	-11.6%	-15.1%
Share capital/cooperative capital/guarantee capital	5,275	5,388	5,324	6,324	6,324	3.7%	0.0%
Other reserves	121,769	121,911	112,204	99,808	103,120	-3.3%	3.3%
Retained earnings or losses	23,199	29,801	44,813	62,595	71,147	25.1%	13.7%
Equity	150,429	158,140	162,521	168,931	180,804	3.7%	7.0%
Balance sheet total	3,387,676	3,512,976	3,565,792	3,717,482	3,647,170	1.5%	-1.9%

Source: Reports to the Danish FSA.

Appendix 2: Financial statements for mortgage-credit institutions at institution level, end 2015

DKK mill.	Nykredit Realkredit	Realkredit Danmark	BRFKredit	Totalkredit	DLR Kredit	LR Realkredit	Nordea Kredit	All
Income statement items (extract)								
Net interest income	5,017	7,064	1,943	4,994	1,724	154	2,791	*23,687*
Dividends from shares etc.	100	0	9	0	1	25	0	*135*
Net fee and commission income	802	-509	244	-2,055	-218	-17	-656	*-2,409*
Net interest and fee income	5,918	6,555	2,196	2,939	1,507	162	2,135	*21,412*
Value adjustments	-235	-441	-270	15	-330	4	124	*-1,133*
Staff and administrative expenses	2,268	678	848	547	216	31	241	*4,829*
Impairments on loans etc.	586	431	186	446	94	11	114	*1,868*
Income from associates and group undertakings	3,165	28	0	0	0	0	1	*3,194*
Profit before tax	3,744	5,071	902	1,961	875	124	1,914	*14,591*
Tax	547	1,188	218	461	206	29	449	*3,098*
Net profit for the year	3,198	3,883	685	1,5	670	94	1,464	*11,494*
Balance sheet items (extract)								
Cash in hand and demand deposits with central banks	351	207	250	0	249	250	609	*1,916*
Due from credit institutions and central banks	624,479	28,434	9,015	15,85	2,713	559	50,916	*731,966*
Lending	550,116	745,131	250,892	570,488	133,038	17,413	385,583	*2,652,661*
Bonds	56,053	59,807	7,909	62,843	11,978	1,059	0	*199,649*
Shares etc.	3,733	0	218	0	55	1,015	0	*5,021*
Holdings in associated undertakings	122	18	0	0	0	0	15	*155*
Equity investments in group undertakings	35,594	129	527	0	0	0	0	*36,250*
Total land and buildings	16	0	402	0	98	0	0	*516*
Other property, plant and equipment	204	5	3	0	5	1	0	*218*
Current tax assets	0	0	2	0	0	3	0	*5*
Deferred tax assets	103	0	0	2	1	7	0	*113*
Assets held temporarily	396	161	393	25	62	0	34	*1,071*
Other assets	10,884	2,693	335	2,302	223	11	705	*17,153*
Accruals and deferred income	191	8	26	7	19	0	4	*255*
Total assets	1,282,458	836,593	269,975	651,517	148,442	20,318	437,867	*3,647,170*
Debt to credit institutions and central banks	17,724	16,611	94	606,415	0	0	24,608	*665,452*
Issued bonds	1,173,411	762,944	254,491	18,368	134,342	16,693	389,568	*2,749,817*
Other non-deriv. finan. liabs. at fair value	427	0	0	0	0	0	0	*427*
Current tax liabilities	16	24	0	26	4	0	29	*99*
Other liabilities	14,124	8,11	3,507	6,089	1,585	257	3,341	*37,013*
Accruals and deferred income	0	0	4	0	2	0	20	*26*
Total debt	1,205,701	787,689	258,101	630,898	135,934	16,95	417,565	*3,452,838*
Total provisions	390	128	92	6	5	0	0	*621*
Subordinated debt	10,907	0	0	2	0	0	0	*12,907*
Share capital/cooperative capital/guarantee capital	1,182	630	1,306	848	570	70	1,717	*6,323*
Share premium account	0	0	102	0	0	0	0	*102*
Accumulated value changes	1	31	36	0	43	0	0	*111*
Other reserves	36,850	48,116	9,652	1,646	3,638	3,203	15	*103,120*
Retained earnings or losses	27,427	0	685	16,119	8,252	94	18,569	*71,146*
Equity	65,460	48,777	11,781	18,613	12,503	3,368	20,301	*180,803*
Balance sheet total	1,282,458	836,593	269,975	651,517	148,442	20,318	437,867	*3,647,170*

Note: Nykredit Realkredit issues bonds which finance lending by Totalkredit. This is included as a receivable from credit institutions in the balance sheet.

Source: Reports to the Danish FSA.

Appendix 3: Changes in capital and overall risk exposure, 2011-2015

						Change	
DKK mill.	*2011*	*2012*	*2013*	*2014*	*2015*	*2011-2015*	*2014-2015*
Tier 1 capital	161,494	162,187	163,959	169,177	175,004	*1.6%*	*3.4%*
Own funds	164,602	165,867	167,643	176,130	188,150	*2.7%*	*6.8%*
Total risk exposure amount	871,528	856,380	857,073	846,659	814,978	*-1.3%*	*-3.7%*
Balance sheet total	3,387,676	3,512,976	3,565,792	3,717,482	3,647,170	*1.5%*	*-1.9%*

Source: Reports to the Danish FSA.

Appendix 4: Financial ratios of mortgage-credit institutions 2011-2015

%	*2011*	*2012*	*2013*	*2014*	*2015*
Total capital ratio	18.87	19.36	19.55	20.8	23.09
Tier 1 capital ratio	18.52	18.92	19.13	19.98	21.47
Common Equity Tier 1 capital ratio	16.64	17.75	18.34	19.06	20.92
Return on equity before tax	3.25	5.84	5.09	5.21	8.35
Return on equity after tax	2.64	4.53	4.01	3.80	6.57
Ratio of op. income to op. expenses	1.55	1.94	1.76	1.81	2.62
Currency position	2.24	1.68	1.32	0.91	0.96
Accumulated impairment loss ratio	0.28	0.30	0.38	0.48	0.44
Annual impairment loss ratio	0.10	0.15	0.19	0.19	0.08
Growth in lending for the year	2.03	2.64	1.13	0.88	2.49
Lending in relation to equity	16.57	16.34	15.91	15.64	14.71

Note: Financial ratios are calculated on the basis of the mortgage-credit institutions which existed in the individual years. Growth in loans for the year is based on nominal values.

Source: Reports to the Danish FSA.