Fixed Income Update Week 38

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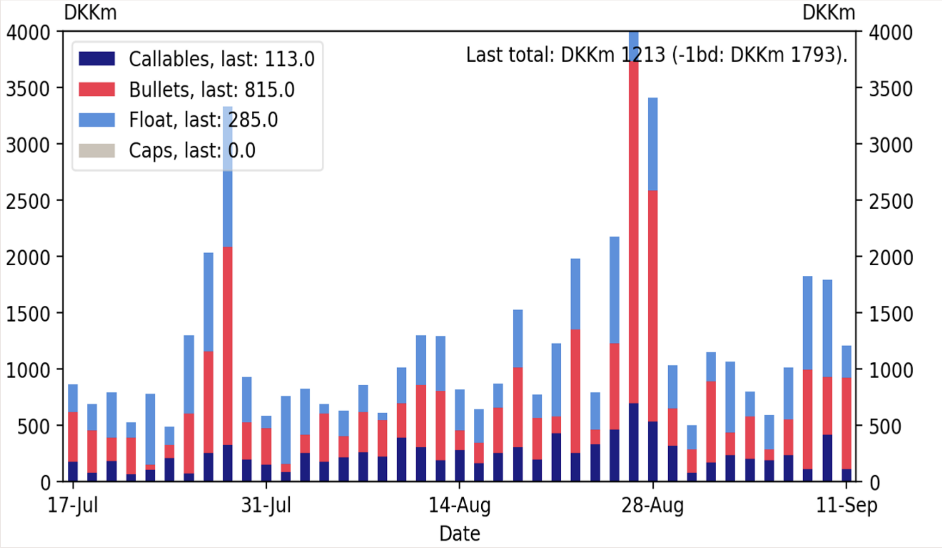
Nykredit

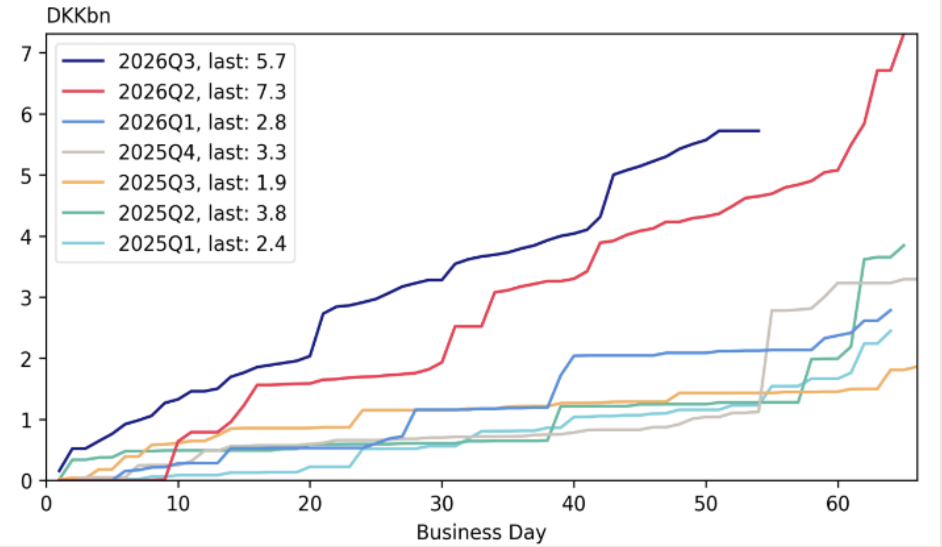
Issuance is picking up again

- As projected, total issuance increased last week after a very quiet start to September. For several days, the daily issuance approached DKK 2 billion, and we still expect volumes to normalise around DKK 1.5-2 billion per day going forward.
- As expected, this progress was mainly driven by higher bullet and FRN issuance, while the issuance of callables remained at a relatively low level.
- Quarter to date, issuance of callables and FRNs is broadly in line with Q2 levels, while bullet issuance is noticeably lower.
- JRK has again in Q3 had great success with "Jyske Frihed", as reflected in another record-high issuance in FRN CIBOR 3M, and we believe the success will continue.
- JRK's additional issuance in the FRN segment has come at the expense of particularly the issuance of 1Y bullets and 3Y bullets, while JRK's issuance of 5Y bullets has remained roughly steady throughout the year.

Daily issuance (OMX)



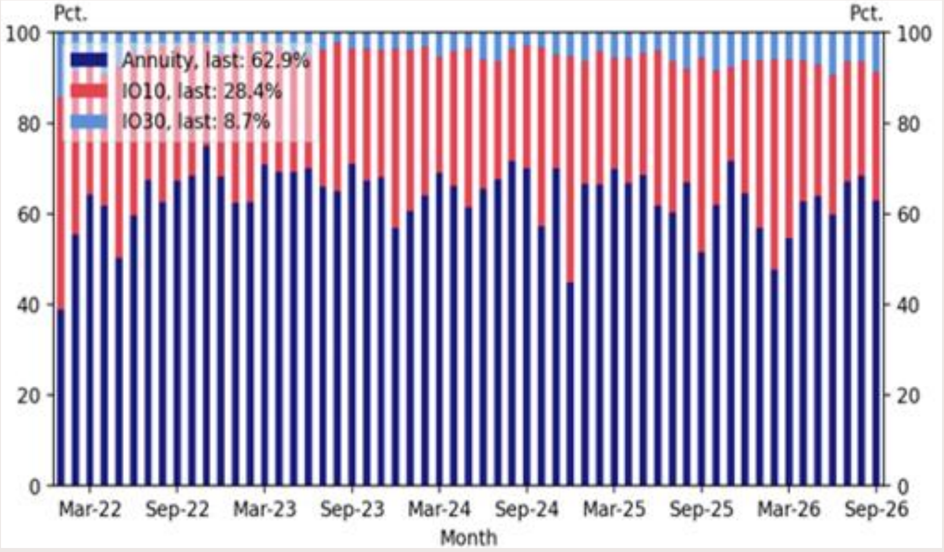
FRN CIBOR 3M: JRK Iss. Net of Refi Auctions (CIRMIL)



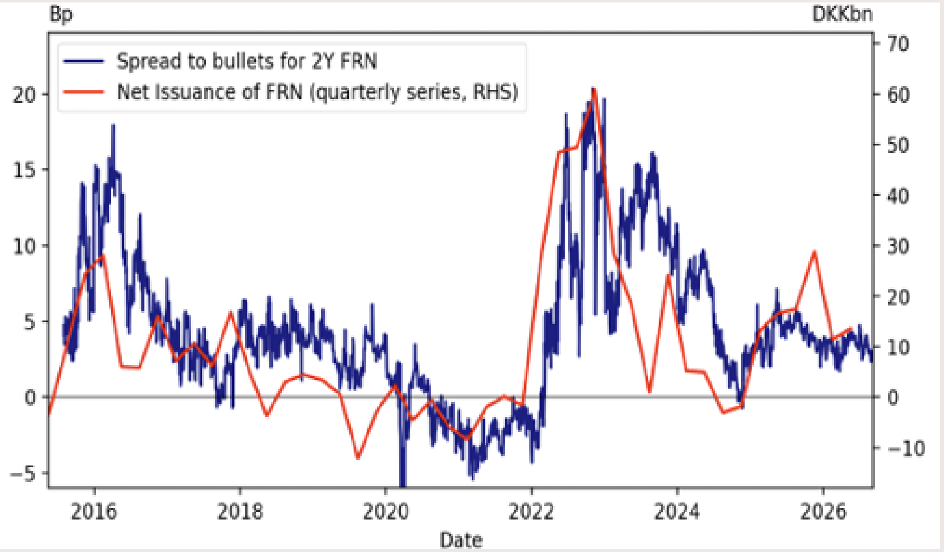
DitRåderum: New Nykredit product

- Nykredit is launching a new product based on a 30-year IO loan financed by Cita 6M FRNs.
- The product also includes a deposit account on which the deposit rate matches the lending rate
- Our immediate expectation is that the product will reduce Nykredit's already low issuance of fixed-rate IO30 bonds, while increasing the issuance of FRNs.
- Initially, we expect the product to put only marginal pressure on the FRN-bullet spread.
- In our opinion, the product may to a large extent compete with secured homeowner loans ("prioritetslån").
- Whether the DitRåderum loan will "kill" the secured homeowner loan remains to be seen, but the product appears aggressively priced.

Callables: Avg daily issuance by month (OMX)



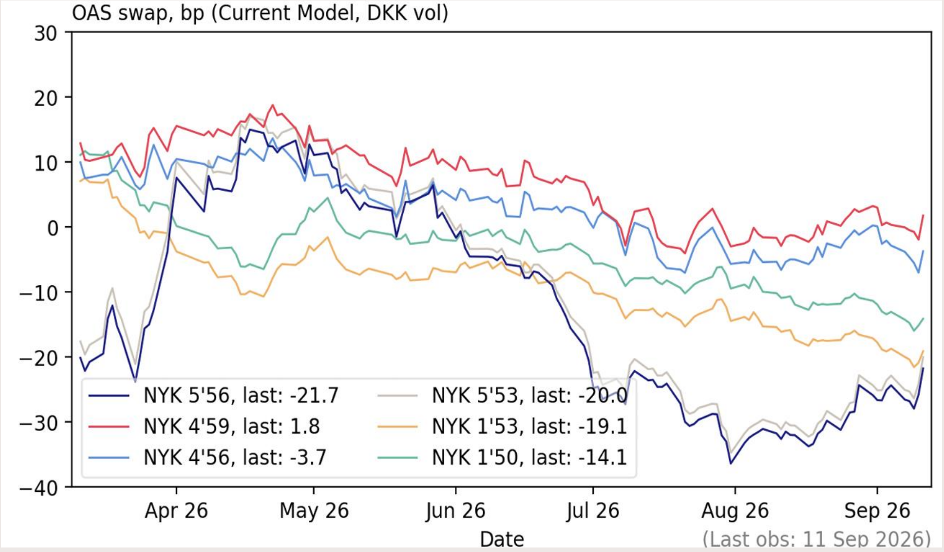
FRN spreads vs bullets and net issuance



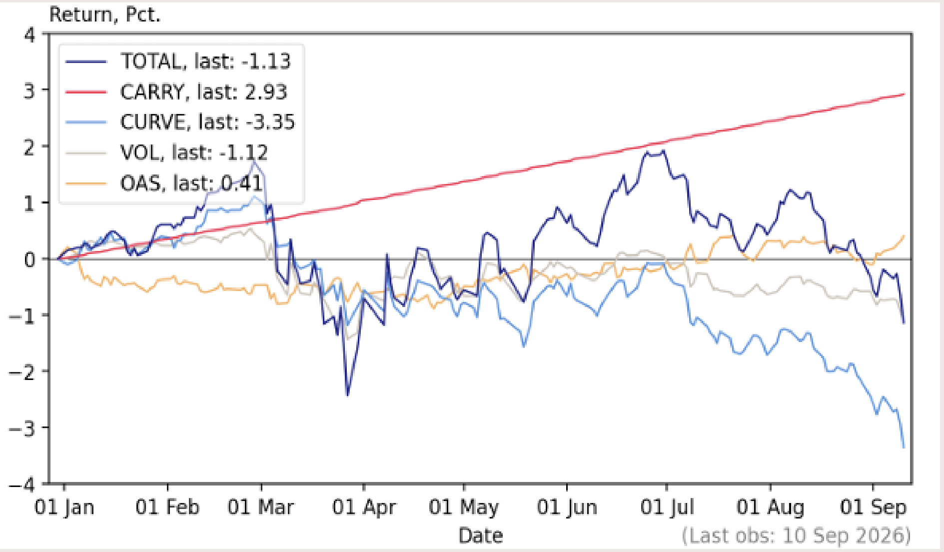
5'59 IO closer than we thought …

- Last week, we argued that bringing 5'59 IO into play would require a +25bp yield increase accompanied by a +5bp vol rise, which at the time seemed unlikely.
- However, we were wrong. ☹
- Over the course of the week, yields and vol increased sufficiently for a 5'59 IO to currently trade at a price of 99.6 – given an OAS of -3bp – while a 5'59 non-IO still remains just above a price of 100.
- NYK and NDA announced this morning the opening of all three 5'59 bonds, and it is our expectation that the other issuers will follow suit in the coming days.
- We have not yet received ISINs for the new 5% bonds.
- The old 5% bonds already lost 5bp last week, and we expect them to continue to lose value today.
- We see scope for spread performance in 4'56, as reinvestment at the October payment date are likely to be directed towards this series given its liquidity.
- Some of this performance potential is, however, likely to be eroded by the full pricing-in of last week's vol rise.
- In the meantime, 4'59 bonds are set to become very small series initially, which is why we have less confidence in spread performance in this series.

30Y callables OAS swap



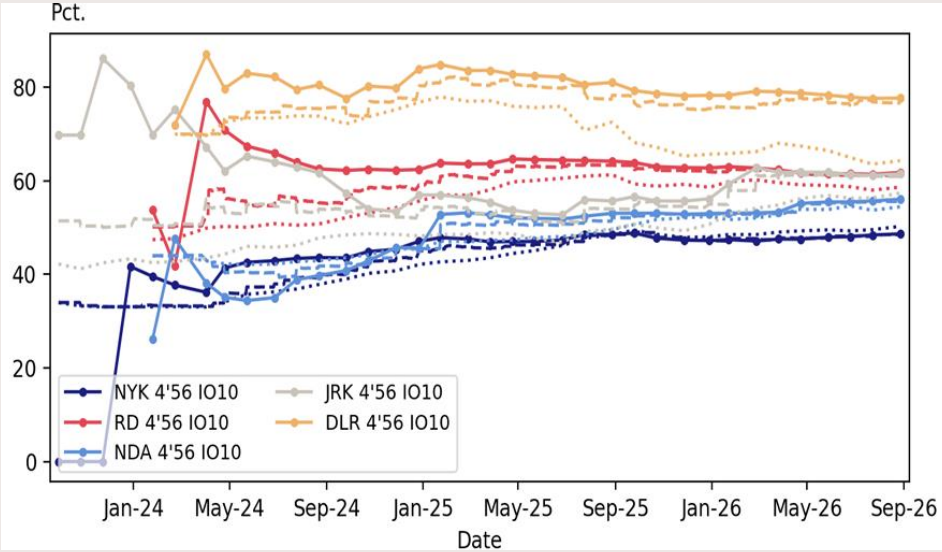
NYK 4'56: Outright



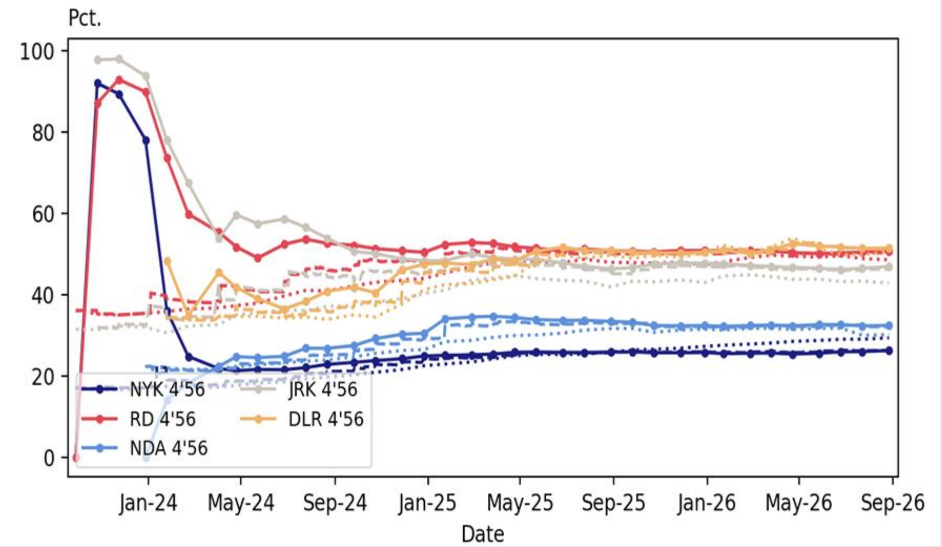
What OAS should 5'59 IO have?

- In connection with the announced opening of 5'59 IO, it is relevant to discuss what OAS these bonds should have.
- At first glance, it seemed reasonable for the bond to trade at roughly the same OAS as 4'59 IO (-2bp), but there are also arguments for both a higher and a lower OAS.
- The argument for a lower OAS is the very low prepayments that have characterised the existing 5% bonds.
- Investors may expect similarly low prepayment rates to affect the new 5% bonds should yields decline again.
- The argument for a higher opening OAS on 5'59 IO is partly the current market turbulence – potentially, we may get many small series with poor liquidity –
- and partly the risk that the initial issuance in the new bonds could be dominated by large loan sizes, as was observed in 4'56 (but not in 4'56 IO) according to the right-hand charts.
- We expect the current market turmoil to result in marginally higher OAS levels for 5'59 IO than the levels at which 4'59 IO is currently trading.

Share of loans over DKK 3 million: CK92 vs CK92NYK



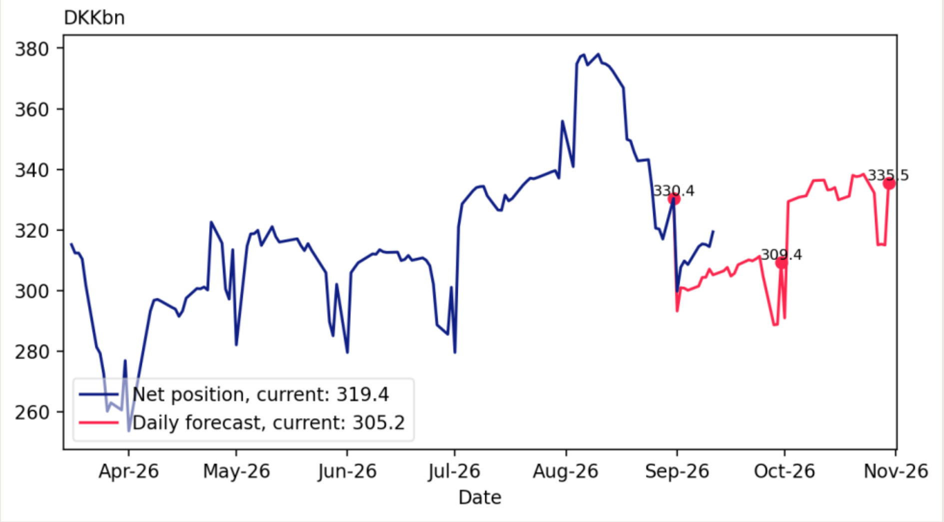
Share of loans over DKK 3 million: CK92 vs CK92NYK



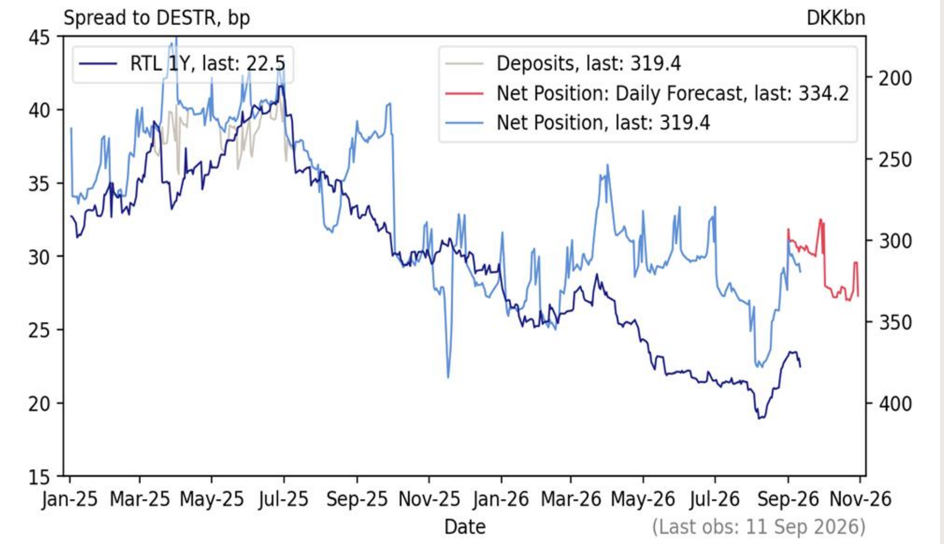
Liquidity

- Thus far, the net position is just under DKK 15 billion higher than indicated by the daily forecast for the government's payments (adjusted for the issuance of government bonds and T-bills).
  - This could be the first sign of the "catch up" in the net financing requirement, which is included in the latest estimate for 2026 from the Danish Ministry of Finance (read more in our latest liquidity analysis here).
  - However, over the past few months, there has been a tendency for the net position to be above the daily forecast at the beginning of a month, only to end the month on a par with or below the forecast.
  - Furthermore, the mentioned "catch up" was not expected to occur until November and December according to the updated monthly forecast.
  - Whether or not this "catch-up" materialises will be important for the outlook for bullets over the next six to seven months.
  - Furthermore, any additional interventions in the FX market by Danmarks Nationalbank could alter the picture. We will be monitoring developments closely!
- In the short term, the net position is projected to increase to around DKK 335 billion in October.
  - This gives bullets a break from the liquidity headwind – at least in the short term. We also saw bullets perform somewhat last week (see also next page).

Net position and daily forecast (incl. issuance)



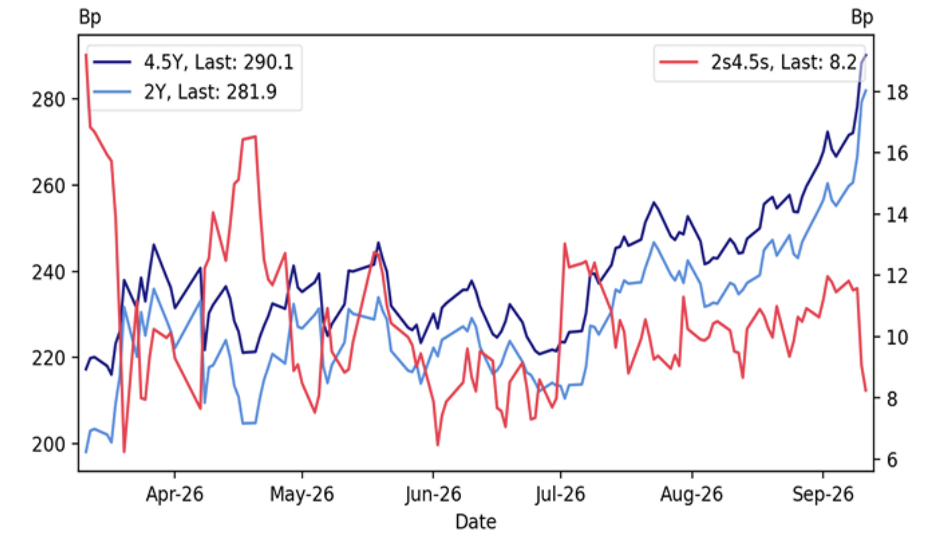
1Y bullets spreads and net position



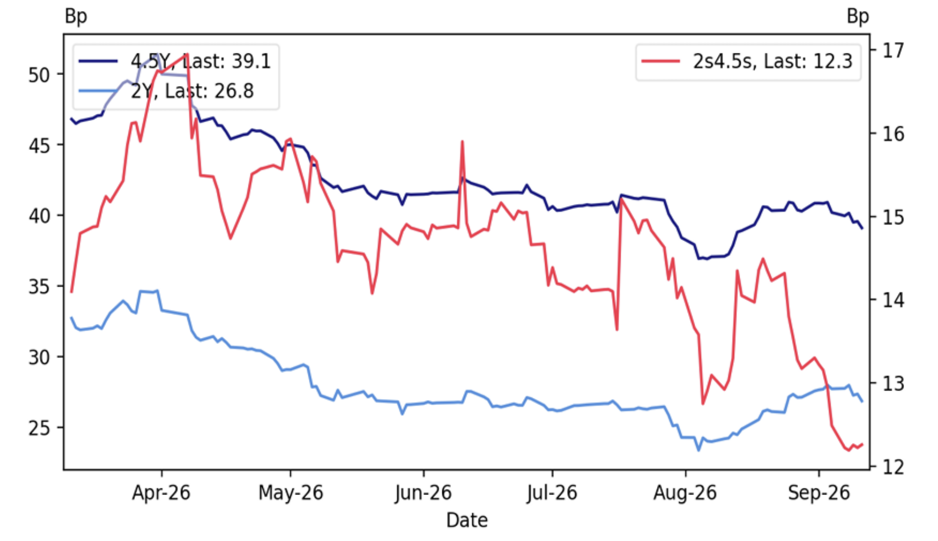
Bullets: Yields up, flatter spread curve

- Last week, we experienced (further) substantial yield rises as well as a flattening of the bullet-DESTR spread curve (2s4.5s).
  - The slope of this part of the DESTR curve has more or less returned to the level seen at the end of June, ie before the significant yield increases of recent months. In the same period, the bullet-DESTR spreads have flattened from about 15bp to about 12bp.
- This flattening of the spread curve makes sense insofar as the hedged and funded return (per unit of spread risk) was somewhat higher for the 4-5Y bullets than for shorter maturities.
  - 4-5Y bullets continue to offer the most hedged and funded return per unit of spread risk.
  - We currently prefer the longer-dated bullets over the shorter-dated ones, see here
- RD has released the first round of preliminary volumes for the November auctions. These comprise just under DKK 31 billion worth of 5Y bullets.
  - However, they currently only reflect the bonds maturing at the January payment date, and the amount of 5Y bullets is expected to tick down considerably towards the deadline for January prepayments (end of October). Still, a fairly large portion of 5Y bullets worth just over DKK 30 billion in total across NYK and RD is expected at the November auctions.
- FRNs have tracked the recent performance of bullets, and FRN-bullet spreads have thus moved sideways.

DESTR OIS

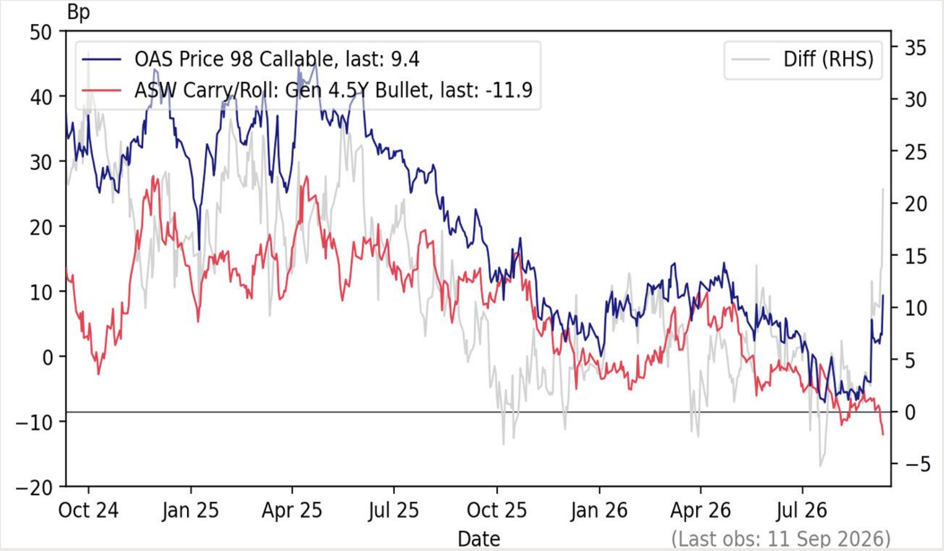


Bullet-DESTR spread

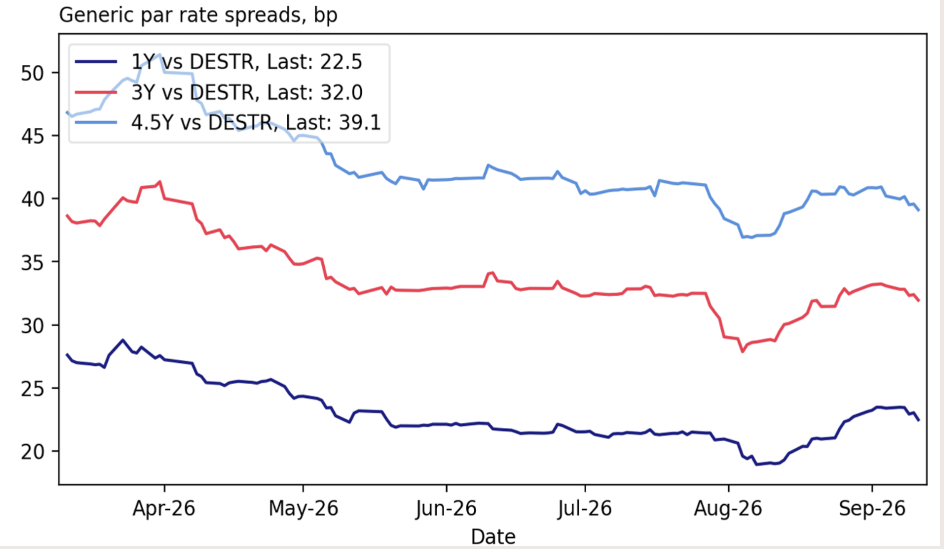


Buy callables over longer-dated bullets

- While last week was tough on callables, bullets gained ground, and we believe that longer-dated bullets have started to look too expensive relative to callables.
- Recently, we have rarely seen the difference between the OAS of a callable bond and the ASW carry/roll-down of longer-dated bullets exceed 5bp for a sustained period (see the top chart; note that the chart reflects the change of maturity class, which makes the difference look more pronounced).
- A generic 4.5Y bullet currently offers just under -12bp in ASW carry/roll-down (CIBOR 6M), while 4'56/4'59 offer an OAS of -3.7bp and 1.8bp, respectively.
- We also believe that the performance of bullets could turn into spread widening in the period ahead, driven by the prospect of a fairly large auction offering in November as well as less support from liquidity (read more here).
- We therefore expect longer bullets to underperform relative to callables.
- We are thus opening a recommendation of 4% callables vs longer-dated bullets on a duration-neutral basis.
- With issuance expected to move into 5'59 IO, we would currently prefer to implement the recommendation in 4'56 rather than 4'59, which initially appears likely to become a very small series.



Bullets: Spreads vs DESTR

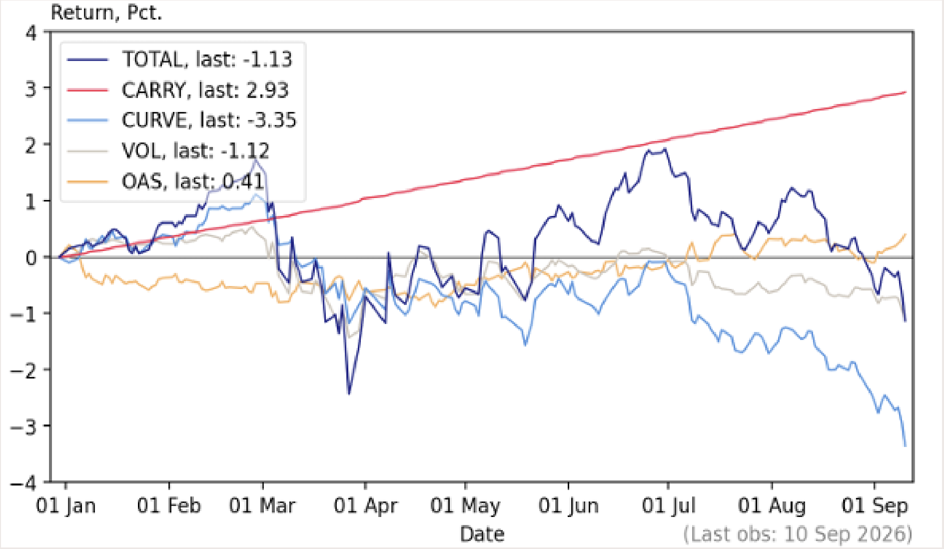


Decomposition of returns

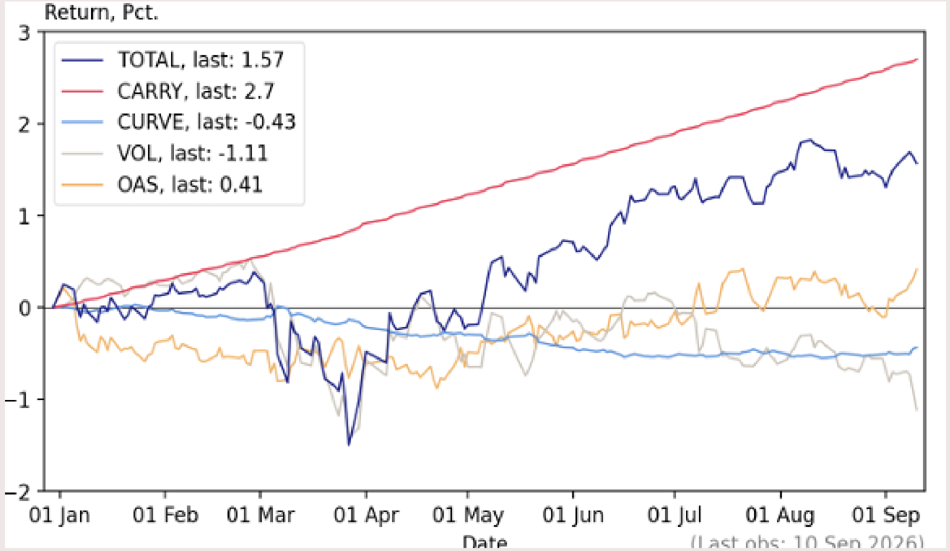
- Last week's yield rise and sharp increase in vol led to massive losses on unhedged callables.
  - Unhedged, 4'56 has delivered a YTD return of -1.1%.
  - Yield exposure hedging would have improved the YTD return by 2.7%.
  - Vol hedging could have improved the return by a further 1.1%.

- From issuance to buyback status?
  - Although 4'56 is not yet a candidate for refinancing into higher coupons, we are approaching the level at which the most aggressive borrowers may start considering refinancing into higher coupons (at a price of 90).
  - However, the "switch-buying" currently seen in 4'56 – presently 0.25% per week – is, in itself, sufficient to support the current pricing and is expected to generate OAS performance relative to OTR bonds.

NYK 4'56: Outright



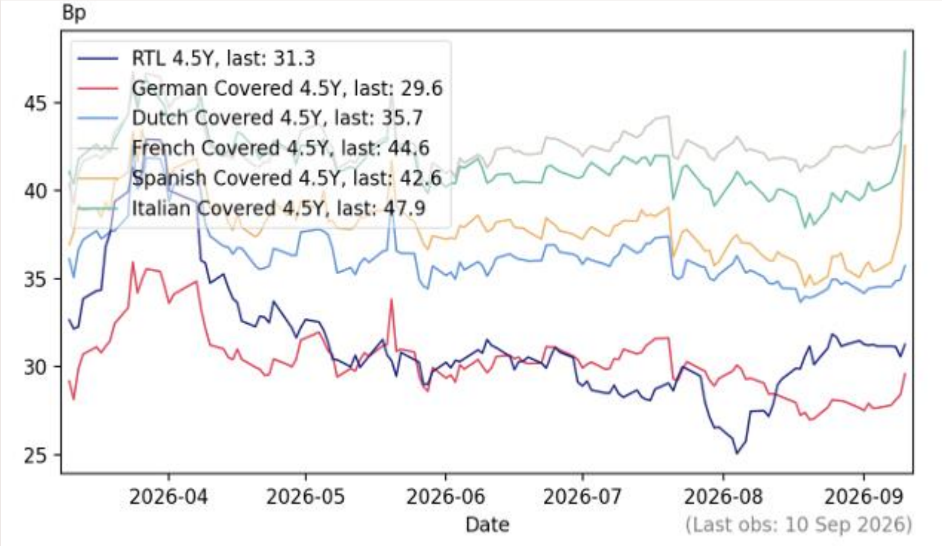
NYK 4'56: Hedged w. 10Y swap



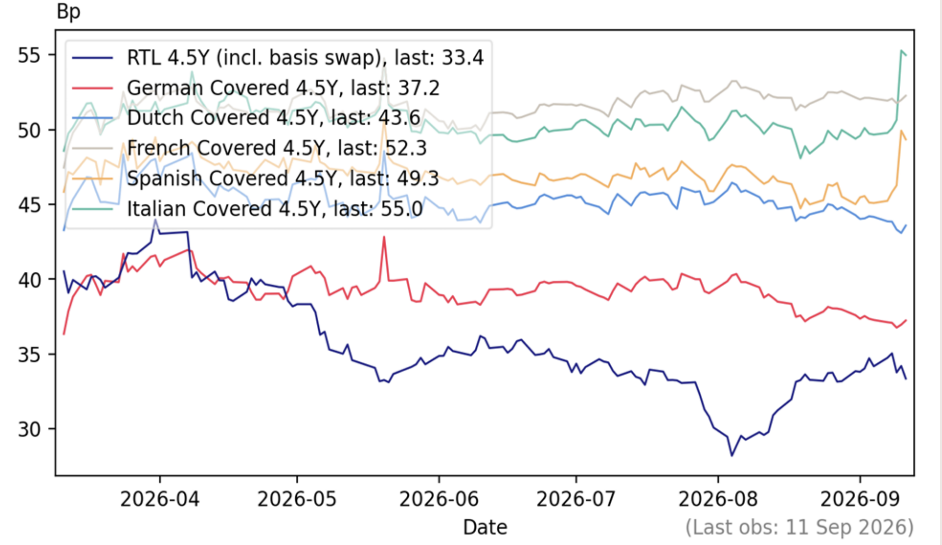
Euro covered bonds

- Higher yields have generally led to bond-swap spread widening in Europe.
- Covered bonds from Spain and Italy have been particularly hard hit.
- Overall, covered bonds have underperformed DBRs, while only Spanish and Italian covered bonds have posted more significant losses vs EUR swaps.

Bullets and EUR covered bonds: Spreads vs DGB/DBR



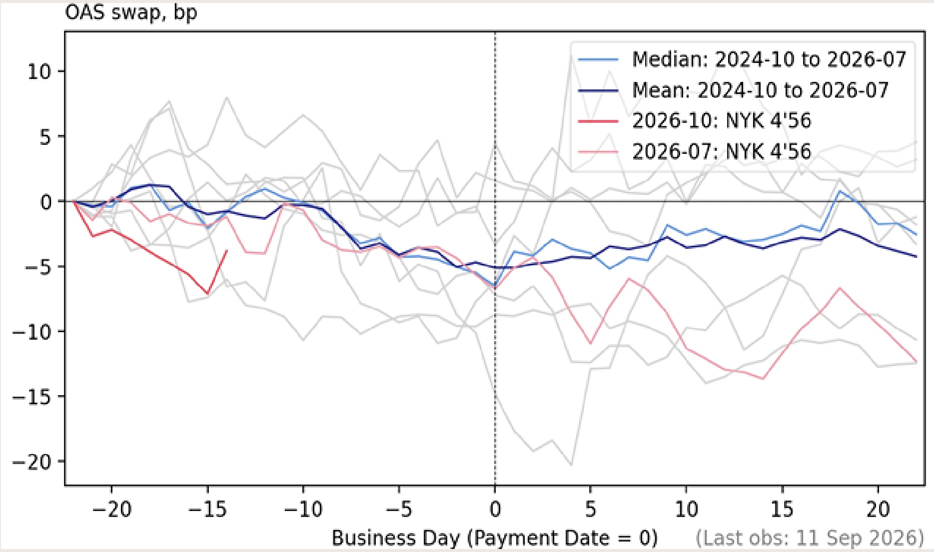
Bullets and EUR covered bonds: Spreads vs ESTR



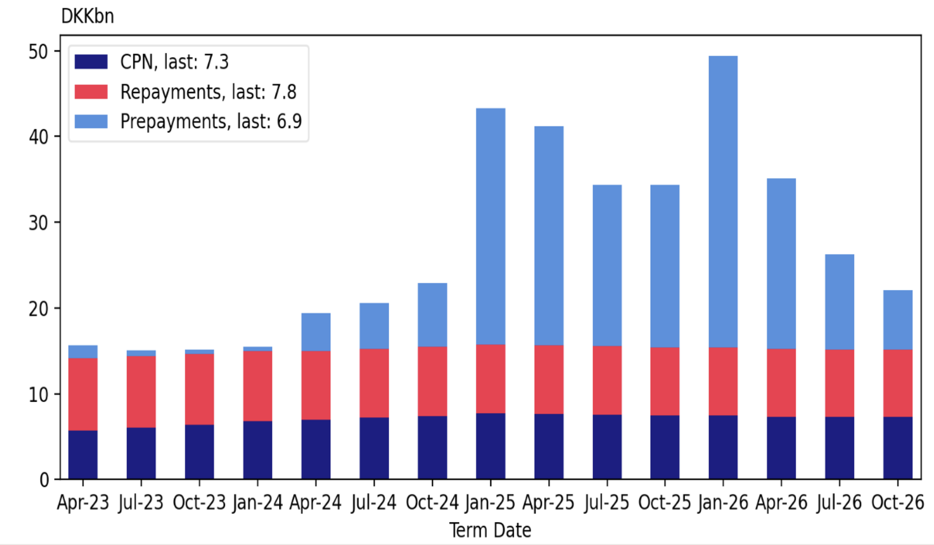
Reinvestment performance?

- We are approaching the October payment date and would therefore normally be entering a period of reinvestment performance.
- But will the current market turmoil eliminate any potential reinvestment performance?
- Once last week's rise in vol has been fully priced into OAS levels, we consider it likely that we will also see performance around this payment date in the old 4% bonds, where we expect reinvestment to take place.
- Any reinvestment performance should mainly occur towards the end of next week.

Reinvestment performance in callables



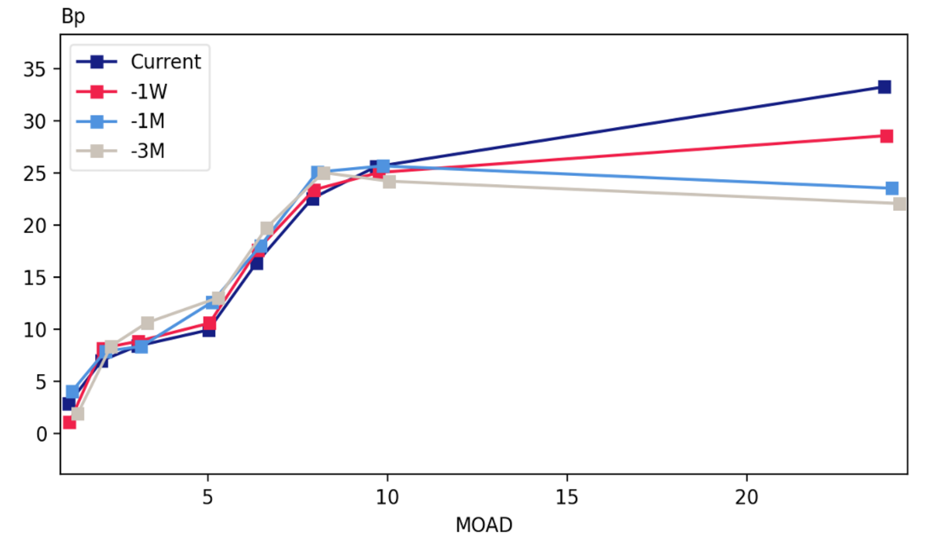
Callables term payments



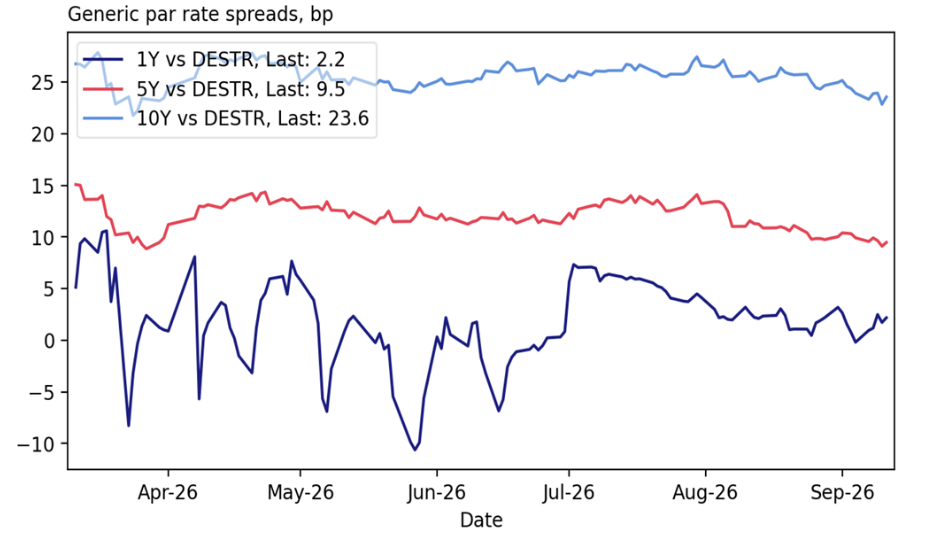
DGB auction: DGB'28 and DGB'35 G

- On Wednesday, DGB'28 and DGB'35 Green will be auctioned.
  - DGB'35 Green is up for auction for the third time this year. In April and June, DKK 1,075 million and DKK 2,250 million were sold, respectively. Thus, there is still considerable headroom to the announced upper limit for green bond issuance of DKK 10 billion.
  - The greenium is not expected to deviate from the 1bp level to which we have now become accustomed.
- DGB'35 is the most attractive point on the government curve in terms of hedged and funded return per unit of spread risk.
  - Spreads vs DESTR have been relatively stable in recent months, albeit with a few basis points of performance in connection with the yield rises and market turmoil seen over the past few months.

DGB: Spreads vs DESTR



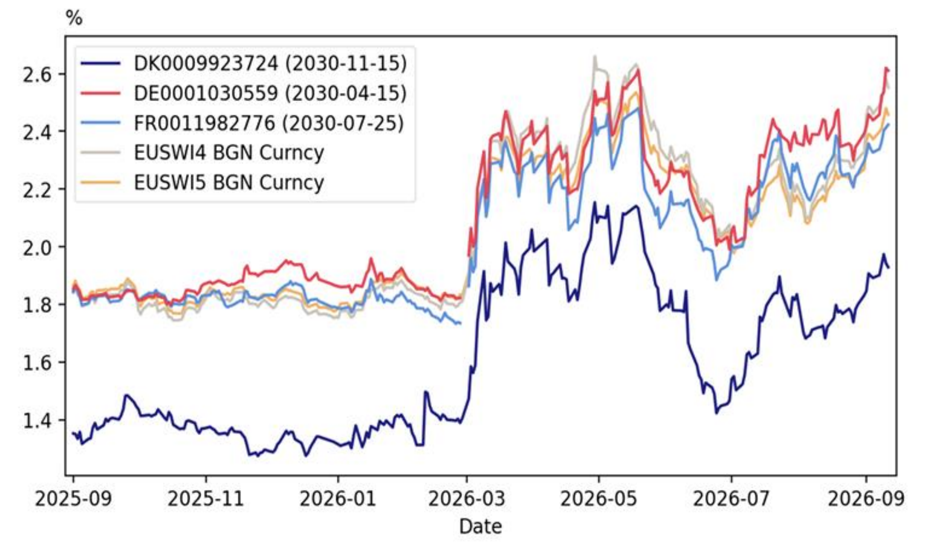
DGB: Spreads vs DESTR



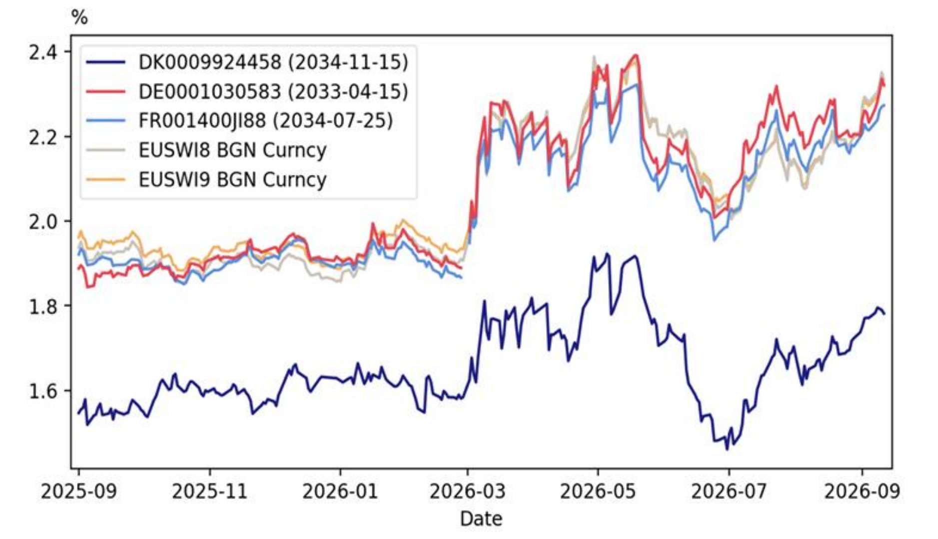
DGBi: Inflation expectations tailwind!

- The latest inflation figures for August showed an increase in inflation, driven mainly by energy prices, but a small decline in core inflation year on year.
  - However, inflation was not far from expectations based on normal seasonal adjustment.
- The rise in inflation expectations over the past few months, linked to higher energy prices, has provided a tailwind for DGBis, which has to a large extent offset the headwind from higher yields.
  - The tailwind has been stronger for DGBi'30 than for DGBi'34 when measured by break-even inflation.
- This has weighed relatively heavily on our recommendation of DGBI'34 vs DGBi'30 (boxed vs nominal government bonds).
  - We have once again seen BEI(sa) on DGBi'30 rise more in line with European inflation swaps and linkers than has been the case for DGBi'34.
  - This has reinforced the view that DGBi'34 appears relatively cheap, and, *all else equal*, a decline in BEI(sa) on DGBi'30 relative to DGBi'34 seems more likely than the opposite. We therefore continue to see value in DGBi'34 vs DGB'30 and maintain the recommendation.
  - The risk, of course, is a further deterioration of the energy crisis, which could push inflation expectations even higher, particularly in the coming years. In that event, this would provide an additional tailwind for DGBI'30 vs DGBi'34.

BEI (SA): DGBi'30 vs IL bonds and swaps



BEI (SA): DGBi'34 vs IL bonds and swaps



Recommendations

- Our recommendations of 4'56 vs a barbell of 5% bonds and low-coupons continue to be a pain trade. So far, the recommendation has been affected by both OAS and vol, but we maintain it for now.
- Our recommendation of RD 4'56 IO vs NYK 4'56 IO, based on the potential for a greater closing effect in RD's 4'56 IO, has moved into the money following the closing. Since we are now past the closing, we close the recommendation.
- On Thursday, we opened a recommendation of 5'59 vs 5Y bullets, which has so far struggled as a result of vol and OAS widening on Friday. We still believe in the recommendation and are maintaining it.
  - However, if the trade was to be made today, we would recommend 4'56 instead, as issuance currently looks set to move into 5'59 IO.
- Our recommendation of 4-5Y German covered bonds vs bullets has fluctuated around zero over the past month.
  - We maintain this recommendation, as we expect bullets to face additional headwinds from liquidity developments over a 6-7-month horizon (see here).

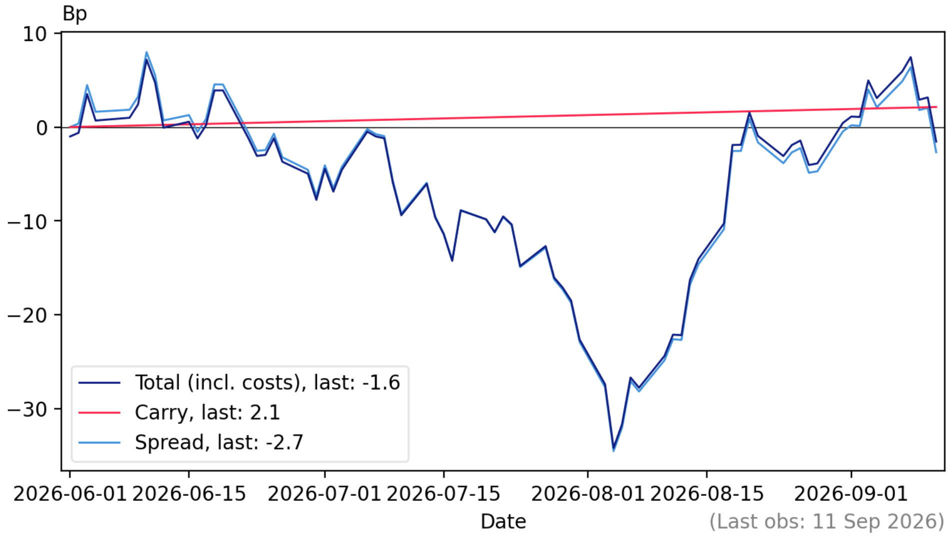
Current recommendations

Opening date	Name	Return 5bd	Total return
2026-06-01	RD 4'56IO vs NYK 4'56IO	-0.00	0.03
2026-06-15	DGBi'34 vs DGBi'30 (BOX)	-0.30	-1.39
2026-07-07	4'56 vs 1'50 & 5'53	-0.22	-0.86
2026-08-21	3Y FRN vs RTL	0.00	0.01
2026-09-02	1'59 vs 4'59	0.14	0.01
2026-09-03	RTL5 vs RTL1 (hedged)	0.01	0.03
2026-09-10	4'59 vs. RTL5	N/A	-0.46

Outlook recommendations

Åbnet	Navn	Afkast 5hd	Afkast total
2025-08-25	CITA vs CIBOR 3M FRN	0.01	0.01
2025-11-27	CIBOR 6M vs CIBOR 3M FRN	-0.03	0.09
2026-01-15	NYK 4'56 vs RD 5'56 + JRK 1.5'53 IO	-0.28	-1.53
2026-01-26	4'56 vs RTL5	-0.54	-0.34

Recommendation: 4.5Y German coverds vs bullets (vs ESTR via basis swap)



Nykredit markets

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BUY: In our view, the bond pricing is fairly cheap relative to comparable alternatives in either the bond or the derivatives market. We expect that the bond will offer a higher return than any alternatives on a horizon of typically three months.

SELL: In our view, the bond pricing is fairly expensive relative to comparable alternatives in either the bond or the derivatives market. We expect that the bond will offer a lower return than any alternatives on a horizon of typically three months.

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Recommendation	
Buy	50%
Sell	50%

As at 13.12.2024
Note: Distribution of our recommendations, which therefore add up to 100%.

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