



Quarterly Report

Fourth quarter 2017

Nordea 1 – Danish Mortgage Bond Fund

ISIN: LU0076315968 (BP-DKK)

Overview

- In Q4 2017, the fund yielded an absolute performance of +0.40%¹, whereas the iBoxx Euro Covered Index, which consists of European covered bonds, posted a return of +0.28%² in EUR terms, and the German government bond index returned -0.33%² in DKK terms
- Outperformance of Danish mortgage bonds versus Danish Government bonds for longer maturities, driven by callables
- New initiative on subsidised housing in Denmark, where subsidised loans will receive a government guarantee and funding will be handled via mortgage bonds

1) Sources: Nordea Investment Funds S.A. and Bloomberg. Period under consideration: 30.09.2017 – 31.12.2017. **The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested.** The fund has no official reference index. For illustration purposes, we have shown the iBoxx Euro Covered Index (IYGB Index) which is an index which consists of European Mortgages, and the German government bond performance index (REXP Index). 2) Source: Bloomberg. Date: 31.12.2017.

Investment strategy

The fund invests a minimum of two-thirds of its net assets in fixed-income and floating rate mortgage bonds issued by private borrowers and public authorities domiciled in Denmark. Investments are made primarily in callable Danish mortgage backed bonds listed on the Copenhagen Stock Exchange. The holdings of Danish mortgage backed bonds in the sub-fund will typically have high coupons in comparison with the general yield level of bonds with similar durations. Investments in Danish government bonds listed on the Copenhagen Stock Exchange are also permitted.

Fund data

Share class	BP-DKK
Fund category	Accumulating
NAV in DKK	235.09
Base Currency	DKK
Fund AUM Million (DKK)	5,764.06
Front end fee in %	Up to 3.00
Annual management fee in %	0.60
Launch date	21.02.1997
ISIN	LU0076315968
Sedol	5206847
WKN	986766
Bloomberg ticker	FRODMBF LX
No. of holdings	90

Data as of 31.12.2017.

Portfolio Managers

Nordea Danish Fixed Income Team



Henrik Stille
Portfolio Manager

Quarterly commentary Q4 2017

Interest rates remained stable in Q4, and over the period Danish long government bond rates were down by around 5bp, while interest rates on medium-dated government bonds were up by around 5bp. The yield curve thus steepened out to the 5-year point and flattened from the 5- to the 10-year point. Danish government bonds slightly outperformed equivalent German Bunds, and the 10-year yield spread narrowed from 8bp to 4bp – a low since the beginning of 2015.

While Danish mortgage bonds generally returned significantly higher than Danish government bonds at the long end of the maturity spectrum, short ARM (adjustable rate mortgage) bonds and short floaters returned in line with short government bonds. Callable mortgage bonds once again delivered the best performance with an excess return of around 1% versus government bonds with a comparable duration. The 1.5% 2047 bond was the top performer with an excess return slightly above 2%, which was attributable to expectations of buybacks.

On the 23rd of November, the Danish government announced a new agreement with mortgage lenders on the financing of loans in the social housing sector. Compared to previously announced proposals, the financing will not be obtained by means of government bonds but instead through government-backed mortgage bonds issued out of a separate capital centre. To ensure optimal cost savings the government may opt to buy the government-backed mortgage bonds and sell comparable government bonds instead. The agreement comprises all borrowing by the social housing sector supported either by the government or by the Danish National Building Fund. The administration and reserve fee still cannot exceed 0.27% of the principal, but mortgage lenders will pay the government a commission of 0.12% of the principal in return for the guarantee. To ensure the quality of the credit assessment, the mortgage lenders will pay a commission of 0.03% of the principal to the government which will be repaid to the mortgage lenders if the government does not incur any losses.

Out of the current subsidised loans of DKK 181bn, ARM bond loans totalling DKK 71bn will be switched into government-backed mortgage bonds when the loans are to be refinanced and fixed-rate loans of DKK 37bn will be switched by mandatory prepayments. Index-linked loans and loans from KommuneKredit will initially not be re-mortgaged. The fixed-rate loans will likely be called faster than initially anticipated and this is positive for the 1.5% 2047 bond, which was up around 1 pct. point on the news. Conversely, high-coupon bonds with a large proportion of subsidised loans, for example 3% 2031 and 3% 2044, saw a negative price reaction.

High-coupon Danish callables moreover came under pressure as prices of re-mortgaging alternatives rose. At the end of November, the issuance in 1.5% 2050 bonds was opened, and issuance gained momentum during December when 2% 2050 bonds traded slightly above par. Higher interest rates towards the end of the month caused prices to drop a tad, and the 2% 2050 was again opened for new issuance. It will be interesting to see, though, whether prices will reach sufficiently high levels in January to kick off a round of switches into lower rates. If so, it will be the first time that borrowers will have the opportunity to switch into a lower-rate 30-year loan (coupon: 1.5%) at an attractive price. This could result in high prepayment activities, notably in 3% and 3.5% bonds.

ARM bonds yielded returns in line with Danish government bonds out to the 3-year point. The 5-year segment yielded an excess return of around 50bp. While demand for short maturities was limited, the appetite for long maturities was fairly strong towards the end of the quarter given the prospect of lower issuance and richer pricing of callable bonds. The 5-year segment saw a spread narrowing versus government bonds of 6bp to 34bp – the narrowest spread since 2014. Conversely, the yield spreads of short maturities widened, and the ARM bonds yield curve thus flattened considerably versus government bonds and interest rate swaps.

Cumulative returns as of 31.12.2017 in %

Time frame	Fund ³
Year to date	2.94
1 month	-0.21
3 months	0.40
6 months	1.82
1 year	2.94
3 years	5.36
5 years	11.49
Since launch	135.09

Calendar year returns in %

Time frame	Fund ³
2017	2.94
2016	4.78
2015	-2.31
2014	6.13
2013	-0.30

Performance (5 year performance)



3) ISIN Code LU0076315968. Inception date: 21.02.1997. Sources: Nordea Investment Funds S.A. Period under consideration: 21.02.1997 - 31.12.2017. The performance represented is historical; past performance is not a reliable indicator of future results and investors may not recover the full amount invested.

Top ten holdings as of 31.12.2017 in %

Company	ISIN Code	Weight
Nordea Kredit 2% 10-01-2047 SDRO 2	DK0002032978	16.50
Realkredit Danmark 2% 10-01-2047 SDRO S	DK0009297194	12.58
Nykredit Realkredit 2% 10-01-2047 SDO E	DK0009504169	9.93
Nykredit Realkredit 2.5% 10 01-2047 SDO E	DK0009798803	4.51
Realkredit Danmark 1% 04-01-2022 SDRO A T	DK0009294928	3.97
Stadshypotek AB 4.5% 21-09-2022	SE0003174838	3.86
Skandinaviska Enskilda Banke 1.5% 15-12-2021	SE0008103477	3.41
BRFKredit 1% 04-01-2020 SDO A E	DK0009390056	3.31
Swedbank Hypotek AB 1% 15-06-2022	SE0007525654	3.14
Danish Government 1.75% 11-15-2025	DK0009923138	3.02

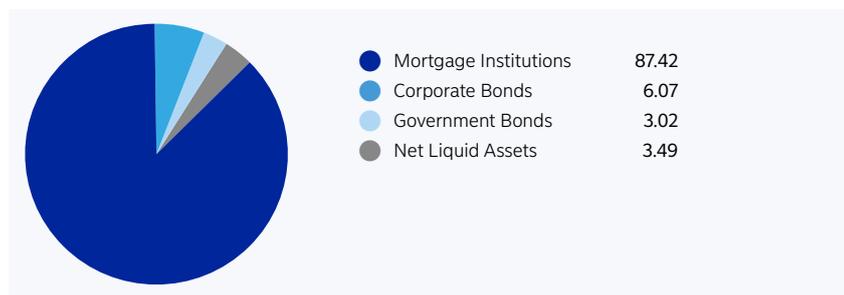
Source: Nordea Investment Funds S.A. Date: 31.12.2017.

Rating breakdown as of 31.12.2017 in %

Rating	Fund ⁴
AAA	89.04
AA	3.86
A	3.41
BBB	0.00
BB	0.00
B	0.00
CCC	0.00
< CCC	0.00
NR	0.20
Net liquid assets	3.49

4) ISIN Code LU0076315968. Inception date: 21.02.1997. Source: Nordea Investment Funds S.A. Date: 31.12.2017.

Asset allocation as of 31.12.2017 in %



Source: Nordea Investment Funds S.A. Date 31.12.2017.

Risk figures as of 31.12.2017

	Fund ³
Effective Duration	4.76
Average Weighted Rating	AAA
Average Weighted Coupon	2.00%
Running Yield	1.92%
Yield to Maturity	1.47%

3) ISIN Code LU0076315968. Inception date: 21.02.1997. Source: Nordea Investment Funds S.A. Date: 31.12.2017.

Maturity breakdown as of 31.12.2017 in %

Years	Fund ⁴
0-3	6.24
3-5	22.08
5-7	0.03
7-10	3.02
10-15	0.08
15-20	0.86
20-25	1.15
25-30	57.91
30-40	5.14
Net liquid assets	3.49

4) ISIN Code LU0076315968. Inception date: 21.02.1997. Source: Nordea Investment Funds S.A. Date: 31.12.2017.

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