"With highly attractive yield spreads to EUR Governments and covered bonds, high liquidity, and AAA credit rating, Danish mortgage bonds offer EUR investors a unique opportunity — and Jyske Capital is one of the few managers specialising in this asset class",

Allan Willy Larsen, Director and Head of Danish Mortgage Bonds at Jyske Capital.

JYSKE CAPITAL

Danish Mortgage Bonds

JYSKE BANK

Overlooked Opportunity in The World's Largest Covered Bond Market

- Denmark Offers Attractive Yields and Diversification Opportunities

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Attractive, Diversifying AAA Opportunities

Jyske Bank's asset management division, Jyske Capital, is a specialist manager in Denmark's - and the World's largest - covered bond market: the Danish mortgage bond market. The Silkeborg-headquartered investment firm oversees more than EUR 39bn of assets across a range of asset classes, including EUR 11bn in Danish mortgage bond strategies for primarily institutional investors in Denmark, the Nordics and Central Europe.

In this article we meet Allan Willy Larsen, Director and Head of Danish Mortgage Bonds at Jyske Capital.

Jyske Capital has over the past year gained strong traction with investors outside Denmark. A leading Swedish institutional investor has built up a EUR 590m mandate in the Jyske's Luxemburg Sicav fund platform, which ensures ongoing FX management and smooth integration with the client's infrastructure.

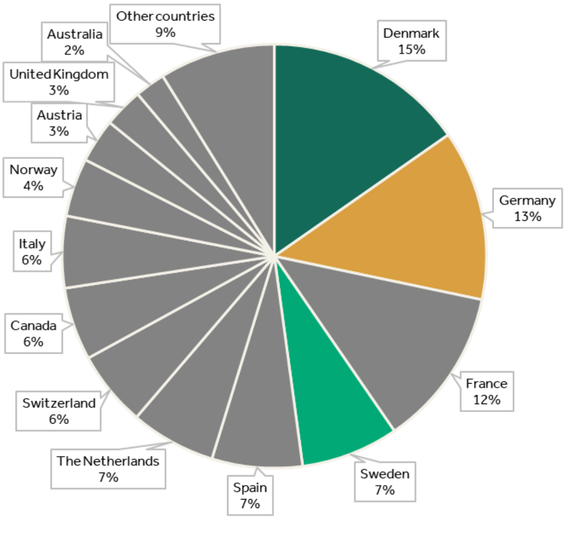
"We see an increased awareness of the opportunity that Danish mortgage bonds can act as a good diversifier in many fixed income portfolios, which often have a significant home-bias", says Larsen.

Please give a short introduction to your team in Jyske Capital and what you see as so special about the Danish mortgage bond market.

"I have been investing in Danish mortgages for 30 years, joined Jyske in 2011 and have led the team since 2015. We are four senior portfolio managers with more than 25 years of average mortgage investment experience. We come with a diverse skillset and a strong collaborative mindset that avoids silos in our work. All managers contribute with their knowledge, quantitative modelling skills, and execution capabilities to create well-founded investment decisions. This leads to robust portfolios."

The Danish mortgage bond market's outstanding volume is as high as EUR 441 bn, according to the latest 2023 ECBC Fact Book, well ahead of Germany and France.

Global Covered Bonds Markets 2023

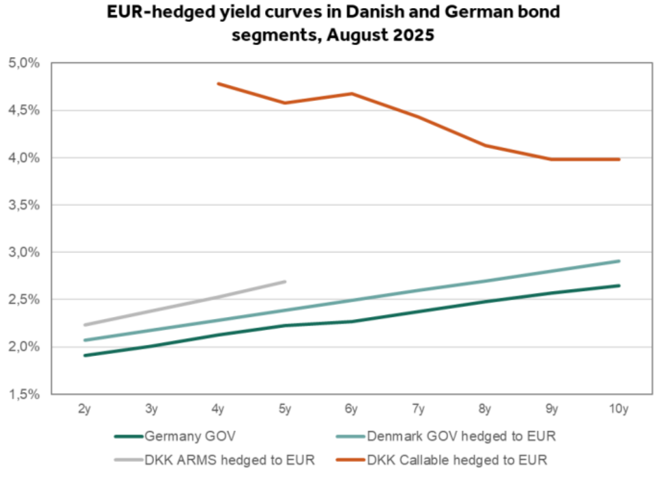


Source: ECBC Fact Book and Jyske Capital

In addition, it has never seen a default in a bond issue, or issuer, since its formation in 1797. The system was literally built upon the ashes of the Great Fire of Copenhagen.

"Many investors outside Denmark consider our mortgage bond market as a classical niche investment, despite its significant volume, high liquidity, a favorable FX hedge to the EUR, and AAA rating. I think it has a lot to do with our unique match funding principle for the funding and different bond types, where the 30-year callable bond is the type most difficult to manage from a valuation and risk management perspective", says Larsen.

What is the investment opportunity, as you see it, and why is it different from what a covered bond investor could get from any other European market?



Source: Jyske Capital and Bloomberg

"Well, firstly, the Danish bond market offers a 0.35 % gain on the FX when hedged to EUR. That means you have a positive head start when comparing with any other European covered bond markets", Larsen begins.

Secondly, he explains that "Denmark offers a diversity of covered bond types, with the long maturity callable segment as the most interesting for European investors.

Here you earn a significant 2 – 3 % p.p. pickup on the Euro covered from the Danish bond's embedded option where the debtor can call the loan on a quarterly basis. In terms of performance, you are close to – or even beyond – the returns of corporate investment grade bonds, but here you invest into an AAA issue", says Larsen.

In Denmark, the mortgage banks are strictly regulated under the "match funding principle". Each loan is matched with bonds from an open issue and sold in the market to institutional investors.

Mortgage banks collect their quarterly interest and downpayments (interest-only loans are also available), retaining only a fee of 0.4% - 1.3% depending on the loan type and the leverage ratio on the property.

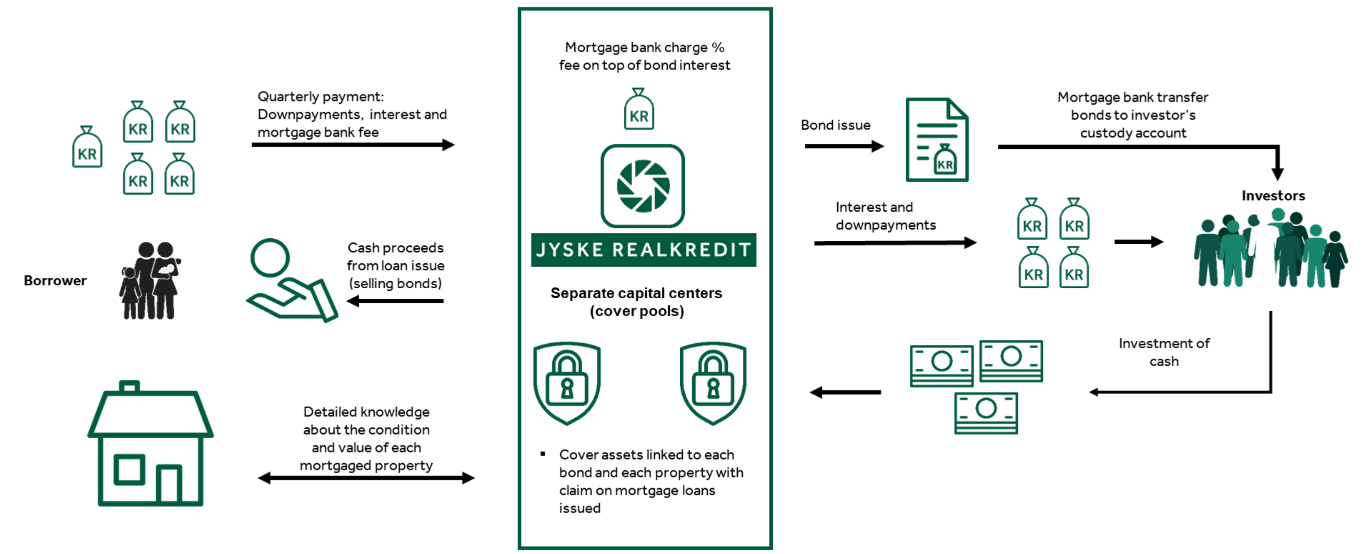
Each bond issue is kept in a cover pool ("capital center") safeguarded and guaranteed by the mortgage bank.

"Investors outside Denmark typically need to spend some time and effort in understanding this unique funding structure for the mortgage loans, being used to the European system where banks issue covered bonds from a "black box" portfolio cover pool.

Here, each capital center has its own AAA rating and cover pool, isolated from the issuer, but with an additional layer of cushion built in from the mortgage banks who must absorb the first losses in case of a crisis. This is why the system is so robust. You may see multiple homeowners who default in a bad scenario, but it never threatens the security of the underlying cover pool of the whole bond issue, which is ultimately what matters to investors", Larsen explains.

Please see an illustration of the match funding principle on the following page.

Match Funding Principle in The Danish Mortgage Bonds System



Source: ECBC FactBook 2023 and Jyske Capital

Why is this market "an overlooked opportunity"?

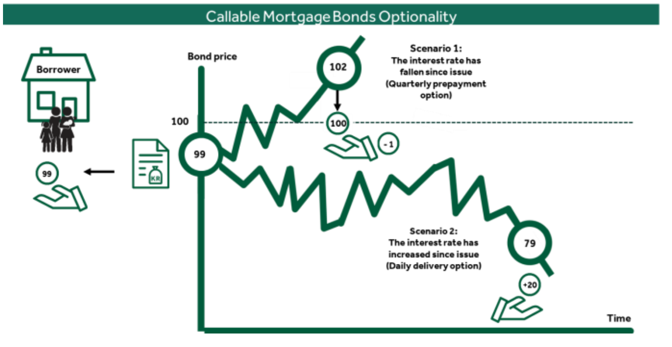
"It's not completely overlooked by sophisticated investors. Actually, foreign ownership of the market has varied over time between 30% - 35%.

That said, it is certainly less sought after by fund managers, asset allocators and pension funds in our neighboring countries like Finland, Sweden, Germany and The Netherlands", says Larsen.

"I believe it comes down to a combination of multiple factors. The most attractive yields are found in the callable segment of the market, which comes with a complex valuation and need for sophisticated risk management due to the negative convexity you introduce by the call option", Larsen continues.

Investors can act every quarter, either calling back the loan if interest rates have fallen, or buying back the bonds tied to the loan in the opposite scenario. This is the function of both the call option in the bond on the one side, and the consequence of the match funding system on the other.

Either way, investors risks getting their investment redeemed much sooner than would be the case with a European covered bond from, e.g. a German bank.



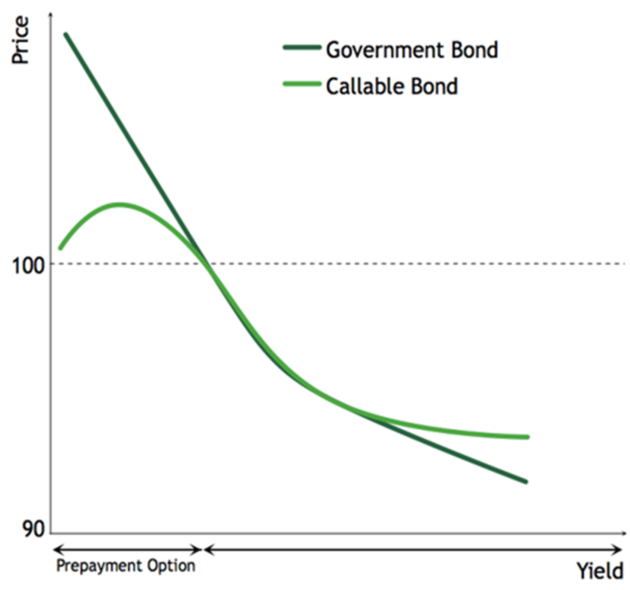
Source: Jyske Capital

Therefore, the complexity of the market needs to be balanced against the sophistication of the fixed income strategy followed by the investors.

"Despite the size of the Danish market, the task of managing valuation and liquidity risks is challenging and therefore costly.

That is why we believe investors are better served with employing a local asset manager who understands this environment and can deliver a robust performance", says Larsen.

Fixed rate callable mortgage bonds – pricing with option



Source: Jyske Capital

Despite the embedded optionality, what are the most important risks factors?

"For Danish mortgage bonds, like other fixed income markets, duration management is the most important risk factor. During the 2022-crisis, where interest rates rose dramatically and fast, many investors found themselves caught by the fall in duration", says Larsen.

What amplified the drawdown, was the tightness of liquidity in an otherwise highly liquid bond market.

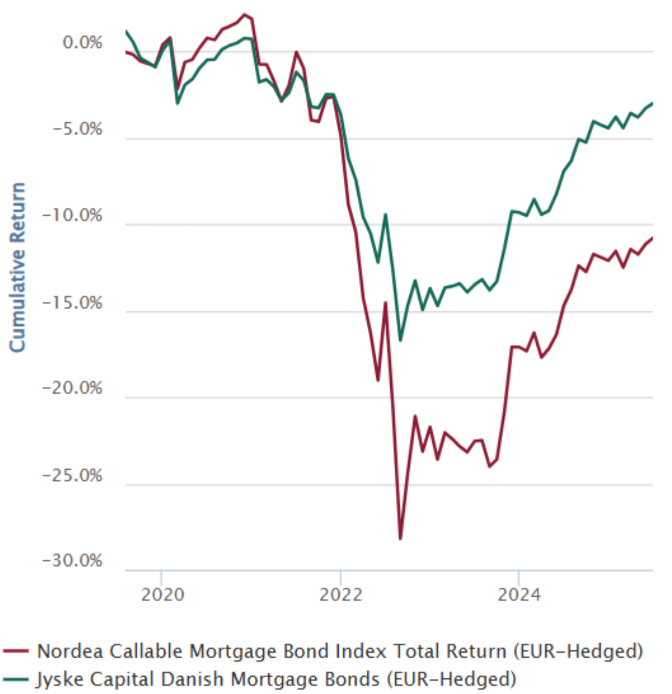
"The Danish mortgage bond market is very liquid; however liquidity is in reality concentrated in large issuing bond series with dozens of smaller issues scattered across maturities and segments with much less liquidity. Some of our peers emphasise the importance of tapping into the liquidity premium obtained from owning such bonds, which works well in a well-functioning market. Until it doesn't't", Larsen continues.

Not only were these positions trapped in face of the rising interest rates that went from 1% coupon on a 30-year fixed rate callable to 5%.

Multiple new issues came to the market during a short time because mortgage banks aways want to maintain new issues at a price just below 100. This has left the market in a situation with very large and very liquid series at opposite spaces in terms of coupons (1% vs. 4% and 5%), and a large number of smaller, illiquid bonds across all segments.

"We have a strong preference for liquidity, because our process is built on an agile value and carry factor approach, where a flexible portfolio is much more attractive than reaping long-term premiums like liquidity", Larsen states.

Return Difference Between a Constant Maturity, Blended Strategy, And a 100% Callable Bonds Index



Source: Jyske Capital

During 2022, some Danish bond strategies with 100% callable bonds lost over -25%, where Jyske's strategy with a blend of callable bonds and traditional adjustable-rate mortgage bonds (ARMS) came though the crisis drawdown far better than most its peers.

“We manage a diverse set of strategies with multiple risk-targets, but the most important factor for us is to ensure that duration is kept within a tight band. Either in absolute terms or relative to a market benchmark. This provides investors with the most transparent risk profiles”, Larsen explains.

The Danish Kroner is managed with a strong peg to the Euro whereas it floats freely relative to the Swedish and Norwegian kroner, requiring investors to manage the FX risk either separately or, like Jyske, within a fund vehicle.

How do investors gain an expected diversification effect when introducing Danish Bonds in a portfolio?

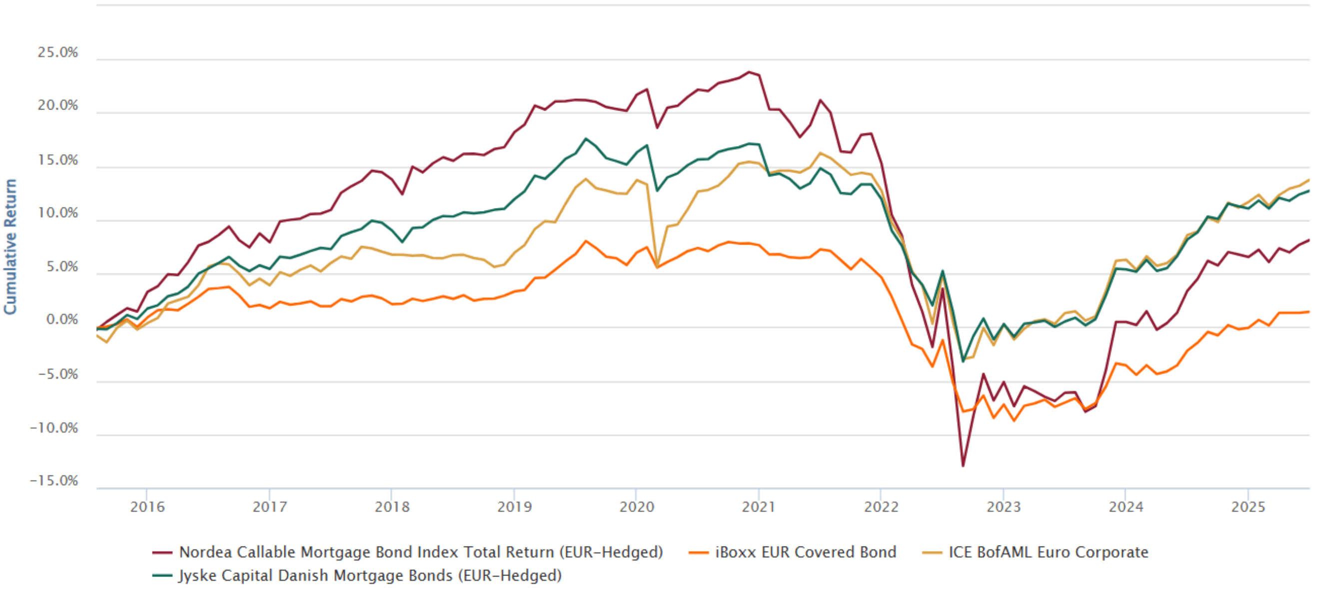
“It’s a tricky question with no clear answer”, Larsen begins.

“It obviously depends highly on the client’s initial portfolio, risk budget and ability to manage the FX risk vs. the Danish kroner. However, we typically see investors who look for the opportunity to diversify on multiple dimensions across a larger fixed income portfolio”, Larsen explains.

When introducing Danish mortgage bonds into an existing European or Nordic investment grade portfolio, you add diversification not only by introducing new bond types (Danish callable, floating rates and adjustable-rate mortgage bonds) but also open for a country effect that exposes the portfolio to the Danish economy and notably its real estate market. Here the underlying structure of the Danish mortgage system comes in, which introduces a different, positive, credit story.

The system is further anchored in tough FSA regulation on the Danish homeowners and debtors, who face material limitations on their leverage relative to not only the house, but their household income too.

10 Years Cumulative Returns from Nordea Callable Bond Index, Jyske Capital Danish Bonds Strategy, ICE IG Corporate and Eur Covered Bond Indices, Period Ending July 2025



Source: Jyske Capital, ICE, iBoxx, Nordea and eVestment. Returns hedged in EUR

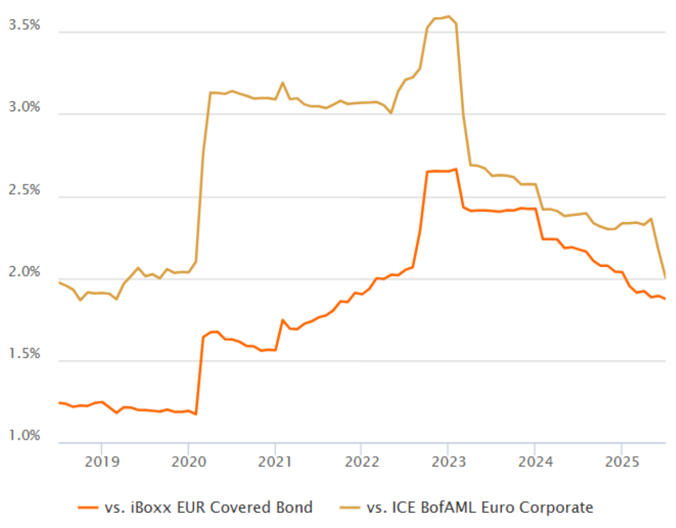
This is enforced by the banks who distribute the loans and minimize the risk of debtor defaults significantly.

"When we analyse different Danish bond strategies with constant maturity benchmarks as a common factor, they all come out strong in terms of returns and standard deviation compared to IG corporate, Euro covered and Euro Government bond benchmarks.

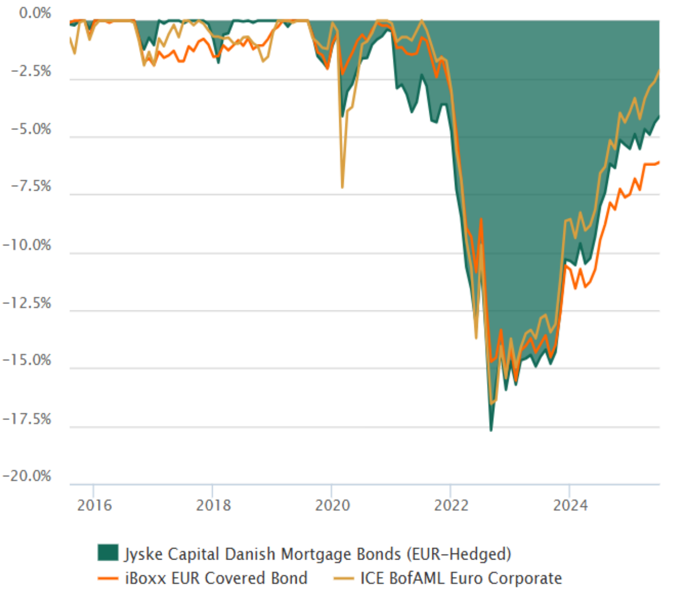
That's a strong argument, especially when you take the AAA rating into account. In addition, we saw a favorable correlation pattern during the environment of rising interest rates in 2019, followed by the Covid-19 crisis, where Danish mortgage bonds both outperformed.

This gives us a good indication that the asset class could help improving the Sharpe Ratio in a diversified fixed income portfolio", Larsen concludes.

3 Years Rolling Tracking Error (vs. Jyske Capital Danish Bonds Strategy) for ICE IG Corporate and Eur Covered Bond Indices, Period Ending July 2025



Absolute Return Drawdown Analysis for Jyske Capital Danish Bonds Strategy, ICE IG Corporate and Eur Covered Bond Indices, Period Ending July 2025



Source: Jyske Capital, ICE, iBoxx, Nordea and eVestment. Returns hedged in EUR

Available Share Classes for Non-Danish Investors

Facts	Jyske SICAV Danish Bonds DKK IC	Jyske SICAV Danish Bonds EUR RD	Jyske SICAV Danish Bonds SEK IC
ISIN	LU1529111228	LU1529111491	LU2755787897
Launch date	01.02.2017	01.02.2017	26.02.2024
Fund AUM	**DKK 4.756.762.883 / EUR 638.491.662**		

Source: Jyske Bank, 12.08.2025. www.jyskesicav.lu