

Time for reinvestment performance - or is it?

Reinvestment performance round #27

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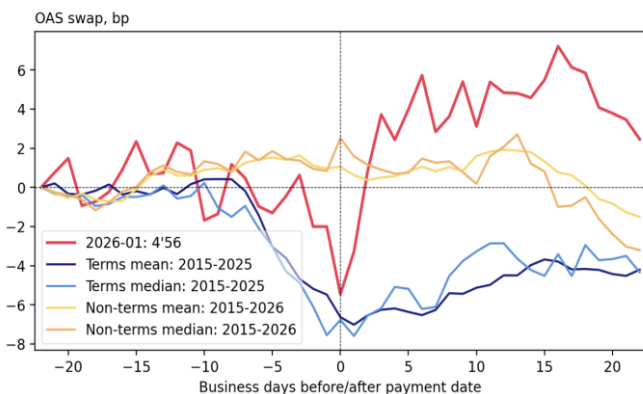
Marketing communication

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- We expect slightly weaker reinvestment performance in callables and normal reinvestment performance in bullets this time
- The reinvestment need is smaller and relative pricing between callables and bullets is more balanced
- The current situation in the Middle East could overshadow everything and end up cancelling the reinvestment performance

We expect reinvestment performance in callables of around 5bp. Despite spread widening over the past few months, we do not see an obvious performance potential. At the same time, a reduced reinvestment need and less negative net issuance mean that the supply/demand situation is more balanced. Therefore, we also believe that fewer investors will reinvest in bullets rather than callables this time, and expect reinvestment performance in the region of the usual 1-2bp in bullets. The war in the Middle East could, however, prove to be the decisive factor in determining whether we will see reinvestment performance this time.

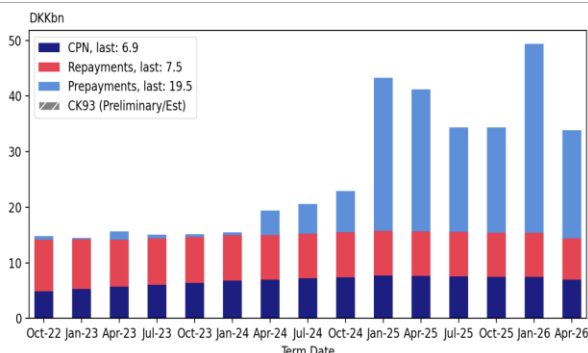
Lower-than-normal reinvestment performance at the January payment date



Reinvestment performance in callables

Source: Nykredit Markets

Smaller reinvestment need this time



Prepayments and principal and coupon payments in callables by payment date

Source: Nykredit Markets

No repeat of January prepayments in sight

Reinvestment performance in callables was somewhat lower than normal in connection with the January payment date, ending at around 4-6bp compared with the 6-8bp that has historically been the case. Meanwhile, reinvestment performance in bullets is stronger than usual (3-4bp in 3Y-5Y bullets compared with the typical 1-2bp normally).

We do not expect January prepayments to be repeated at the April payment date.

Lower reinvestments and less expensive callables

We attribute the stronger reinvestment performance in bullets and the correspondingly lower reinvestment performance in callables last time primarily to the expensive pricing of callables at that time.

We believe that this has dampened the performance potential in callables and, at the same time, prompted some investors to reinvest in longer-dated callables instead, thereby giving rise to greater reinvestment performance there.

We do not expect the same degree of reinvestment performance in bullets this time. Firstly, the spread widening over the past few months means that callables are not nearly as expensive. Secondly, the reinvestment need has eased, and the total net issuance of callables for the quarter is less negative than last time (expected DKK -3 to -8 billion compared with DKK -16 to -18 billion). Furthermore, longer-dated bullets continue to trade at tighter spreads – despite recent weeks' spread widening – than they did ahead of the January payment date. As a result, the case for reinvesting into bullets rather than callables is less compelling this time.

We therefore do not expect significant reinvestment performance in bullets, but rather a repeat of the usual pattern in which they "only" recover what they lost in the period up to the end-of-quarter issuance.

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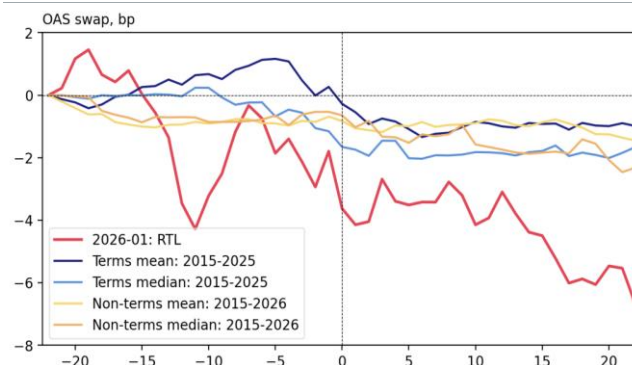
Historically, payment dates have tended to generate performance of around 6-8bp in OTR callables (see the upper chart). We find it hard to see scope for a comparable degree of reinvestment performance. Despite the spread widening since the turn of the year, we do not see an obvious performance potential in callables. At the same time, the net issuance is less negative than in many of the previous quarters. So while there is still potential for reinvestment performance, we expect it to be at the lower end – around 5bp.

Reinvestment may need to be cancelled altogether

Our expectations should, however, be viewed with the caveat that the current situation in the Middle East may trigger additional volatility and upward pressure on yields, as well as weaker risk appetite. In other words, the conflict may overshadow the payment date entirely – meaning that we may see no reinvestment performance at all this time.

A calming of the conflict, on the other hand, could trigger a reversal of the spread widening seen over the past week and a half – making any reinvestment performance appear more pronounced.

Exceptionally strong reinvestment performance in 5Y bullets last time!



Reinvestment performance in bullets

Source: Nykredit Markets

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Recom- menda- tion	
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As at 13.12.2024

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

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