

Bank of England

Prudential Regulation Authority

Review of Solvency II Effective Value Test parameters – applicable from 30 September 2022

The parameters to be used in the Solvency II Effective Value Test (EVT), as set out in Supervisory Statement 3/17,¹ have been reviewed and updated as set out below.

The parameters in this document apply from 30 September 2022. When conducting the EVT, all firms should use a deferment rate greater than or equal to the minimum rate published by the PRA, along with the volatility parameter set out below.

Deferment Rate Parameter

The minimum deferment rate in Policy Statement 31/18² as of December 2018 was 1% per annum, which was reduced to 0.5% per annum in September 2019 following a review of movements in long-term real interest rates. For the review in September 2022, the PRA has again examined long-term real interest rates, measured using a range of swaps-based data sources, at a range of long-term tenors from 10 to 30 years. Having taken into account current market conditions, the PRA's judgement, informed by this analysis, is to increase the minimum deferment rate used in the EVT from 0.5% to 2% per annum.

The PRA will keep the minimum deferment rate under review.

Volatility Parameter

The PRA has analysed house price indices from Nationwide and the Office for National Statistics up to Q1 2022. A time series model was fitted to quarterly log-returns from each of these indices to derive values for long-term index volatility. These values were

¹ PRA Supervisory Statement 3/17 'Solvency II: illiquid unrated assets', April 2020:

<https://www.bankofengland.co.uk/prudential-regulation/publication/2017/solvency-2-matching-adjustment-illiquid-unrated-assets-and-equity-release-mortgages-ss>.

² PRA Policy Statement 31/18 'Solvency II: Equity release mortgages', December 2018:

<https://www.bankofengland.co.uk/prudential-regulation/publication/2018/solvency-ii-equity-release-mortgages>.

then adjusted to incorporate the effect of idiosyncratic behaviour of individual properties (using data from the Land Registry).

As a result of this analysis, the PRA has decided to retain a value for the volatility parameter to be used in the EVT of 13%.

September 2022