



## Review of Solvency II Effective Value Test parameters – applicable from 31 December 2019

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

The parameters in this document apply from 31 December 2019. Firms that have elected to use a minimum deferment rate of 0% to conduct the EVT prior to 31 December 2021 may continue to do so, notwithstanding the minimum deferment rate published below. When conducting the EVT, all firms should use the published volatility parameter below regardless of the minimum deferment rate they are using.

### Deferment Rate Parameter

The minimum deferment rate in Policy Statement 31/18<sup>2</sup> as of December 2018 was 1% per annum. For the review in September 2019, the PRA has 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. The PRA found that long-term real interest rates had fallen considerably since December 2018, by more than 0.5 percentage points but less than 1 percentage point. The PRA's judgement, informed by this analysis, is to reduce the minimum deferment rate used in the EVT from 1% per annum to 0.5% per annum.

The PRA will keep the minimum deferment rate under review.

### Volatility Parameter

The PRA has analysed house price indices from the Office for National Statistics and the Nationwide Building Society. 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 then adjusted to incorporate the effect of idiosyncratic behaviour of individual properties, using data from the Land Registry.

The PRA's judgement, informed by this analysis, is to retain a value of 13% per annum for the volatility parameter to be used in the EVT.

September 2019

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<sup>1</sup> 'Solvency II: Matching adjustment – illiquid unrated assets and equity release mortgages', September 2019: <https://www.bankofengland.co.uk/prudential-regulation/publication/2017/solvency-2-matching-adjustment-illiquid-unrated-assets-and-equity-release-mortgages-ss>.

<sup>2</sup> December 2018 (page 1 of 2): <https://www.bankofengland.co.uk/prudential-regulation/publication/2018/solvency-ii-equity-release-mortgages>.