



Review of Solvency II Effective Value Test parameters – applicable from 30 September 2020

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 2020. 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 Effective Value Test, 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 31/18² 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 2020, 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. The PRA's judgement, informed by this analysis, is to retain the minimum deferment rate used in the EVT at 0.5% 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 2020. 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).

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

September 2020

¹ '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>.

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