



Society of Actuaries in Ireland

Equity Release Mortgages: Irish and UK Experience

28 March 2019

Disclaimer

The views expressed in this presentation are those of the presenters (Tony Jeffery & Andrew D Smith) and not necessarily of their current or former employers, nor of the Society of Actuaries in Ireland.

What is an Equity Release Mortgage?

- Loan taken out by a property owner, secured on the property.
- The loan is repaid when the borrower dies (or goes into long-term care).
- Interest (eg at 5% pa) is often rolled up on the loan balance so the borrower, while alive, makes no interest payments.
- No-negative-equity guarantee (NNEG): if loan balance on death exceeds the house value, then lender suffers the shortfall.

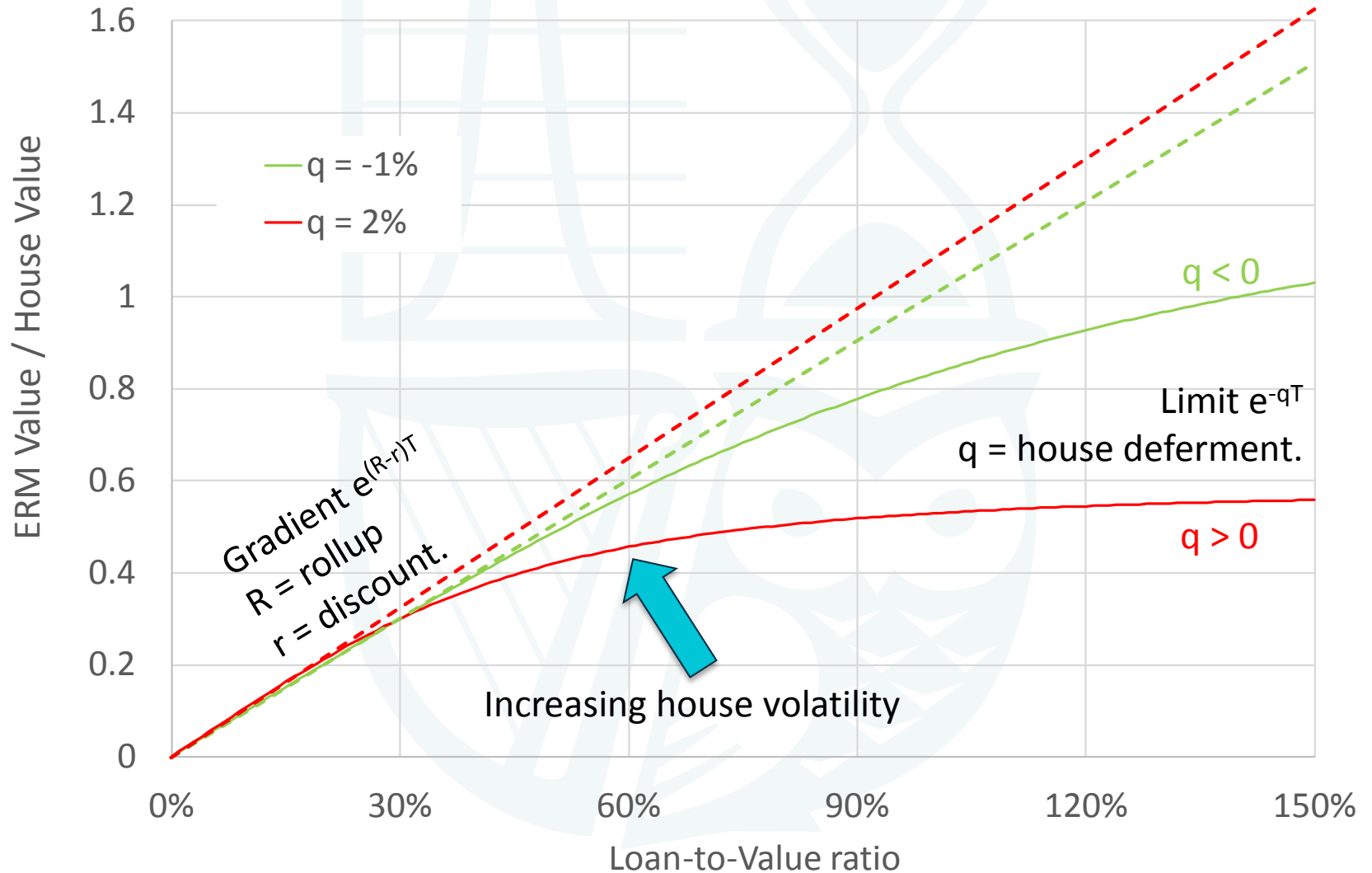
How big is the Market?

- The ERM market has grown substantially in the UK; in 2018 alone nearly £40bn was lent, mostly on behalf of bulk annuity companies.
- Irish market is (disproportionally) smaller; no recent lending and outstanding balances around €300m.

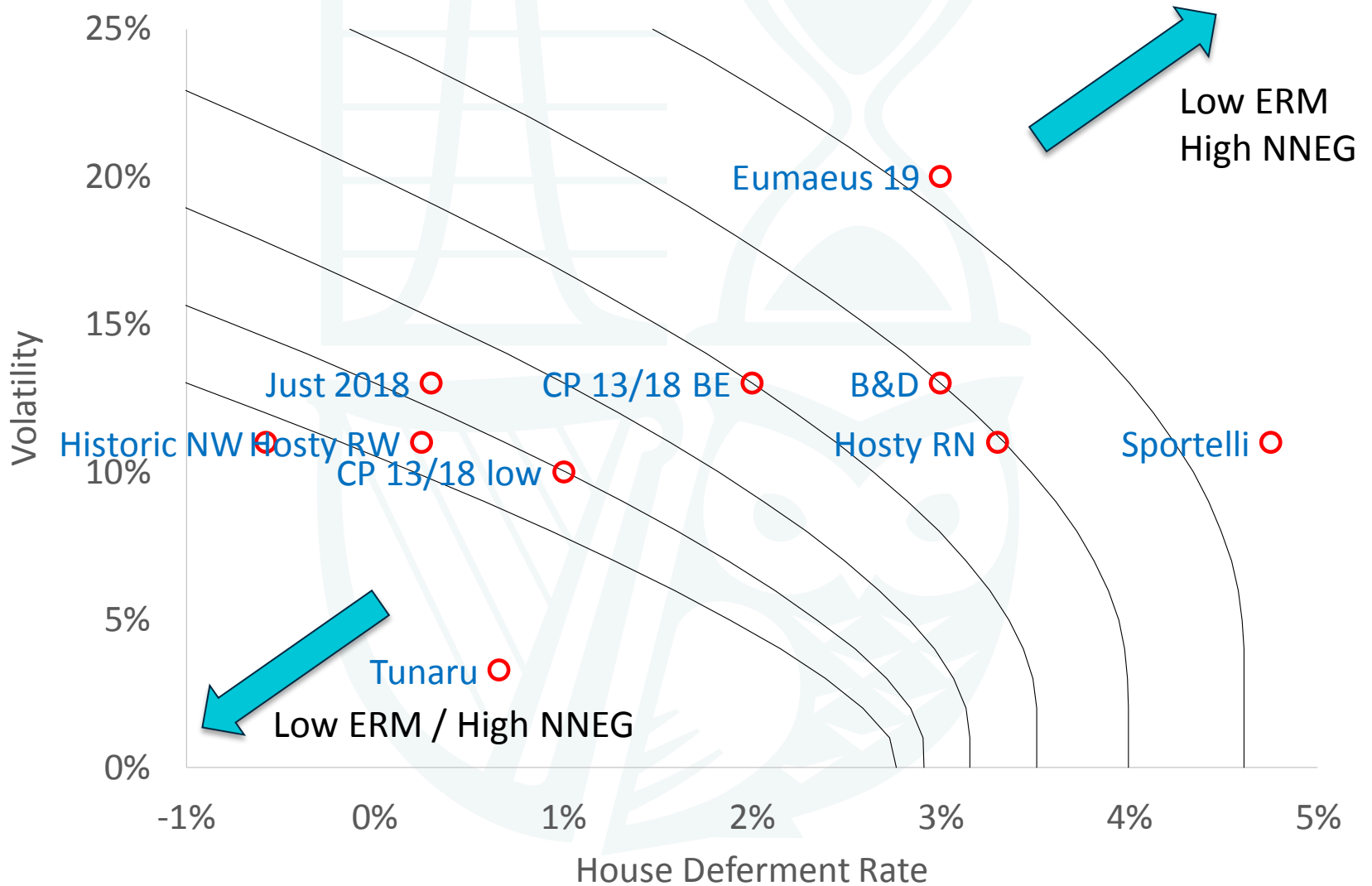
UK Regulatory History: Discounting Annuities

- Solvency I reliable yield; uses assets held.
- Solvency II discount rate has evolved.
 - Liquid risk-free rate
 - Plus volatility / matching adjustment (MA)
- ERM's initially excluded from SII MA
 - But now permitted with some restructuring
 - Discount rate boost higher for ERM's (2%) than any other asset class.
- Ongoing NNEG valuation debate, with PRA on one side and Insurers + IFoA on other.

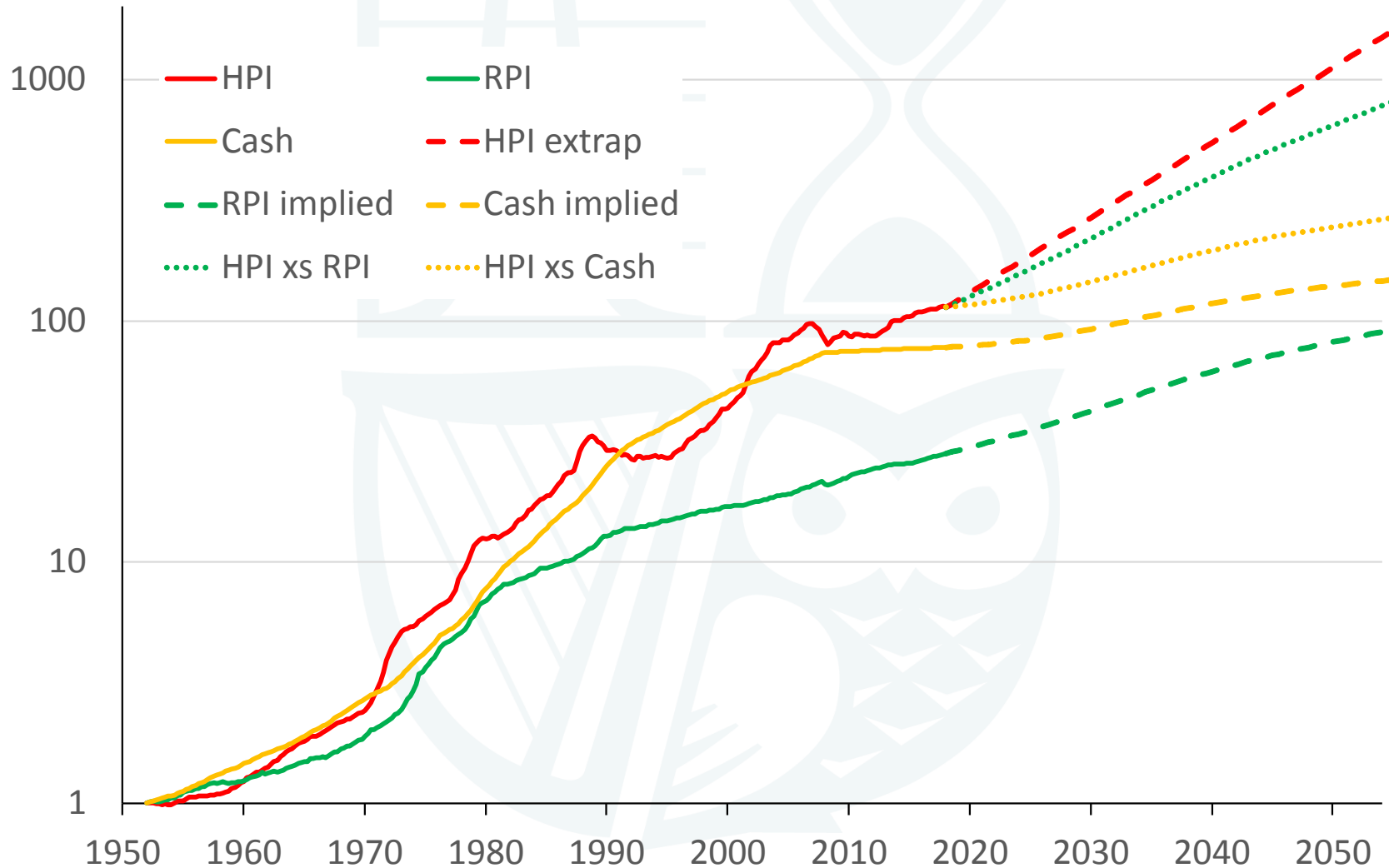
Key Valuation Assumptions (death fixed at T)



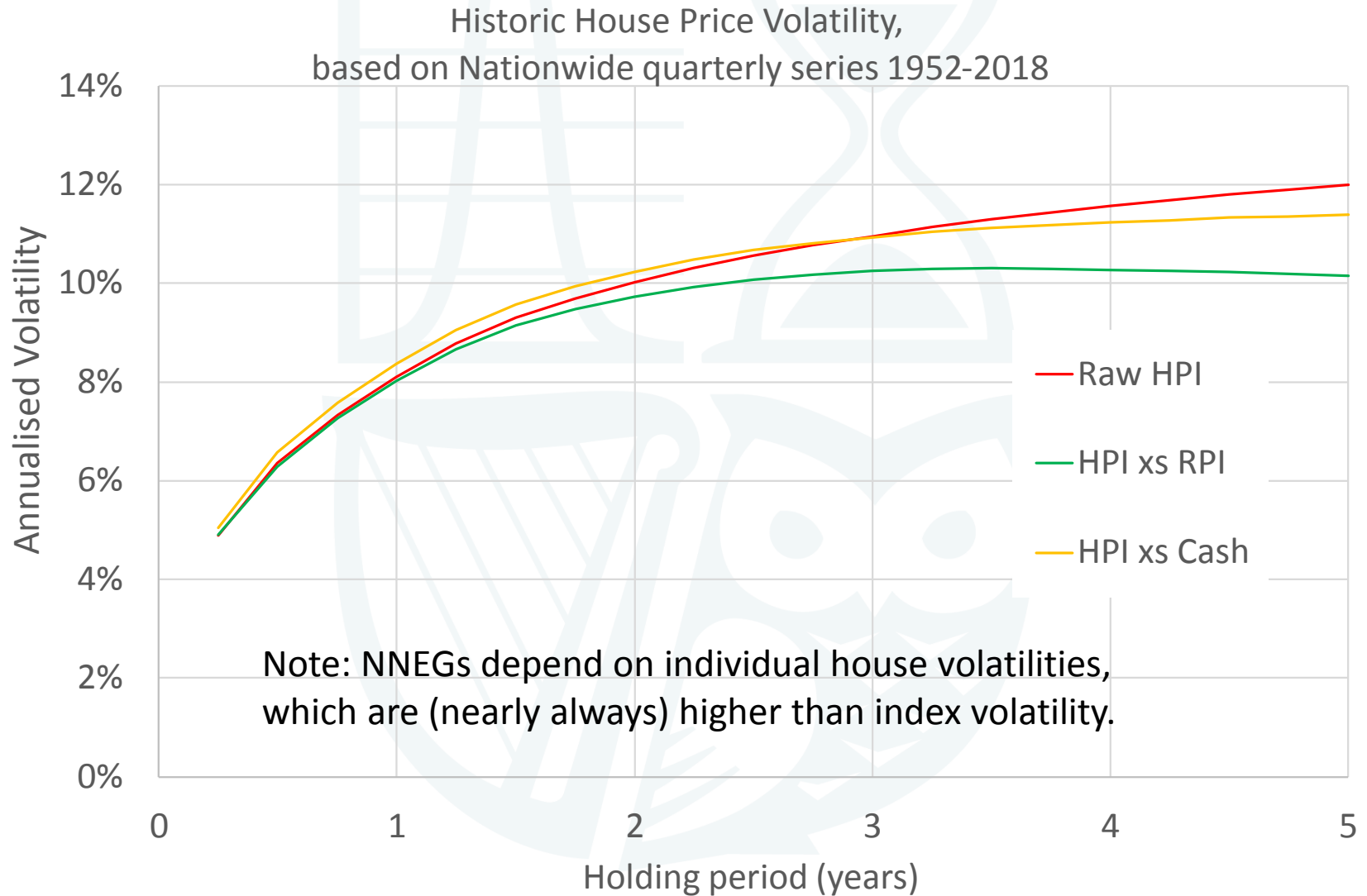
Assumptions and Valuation Contours



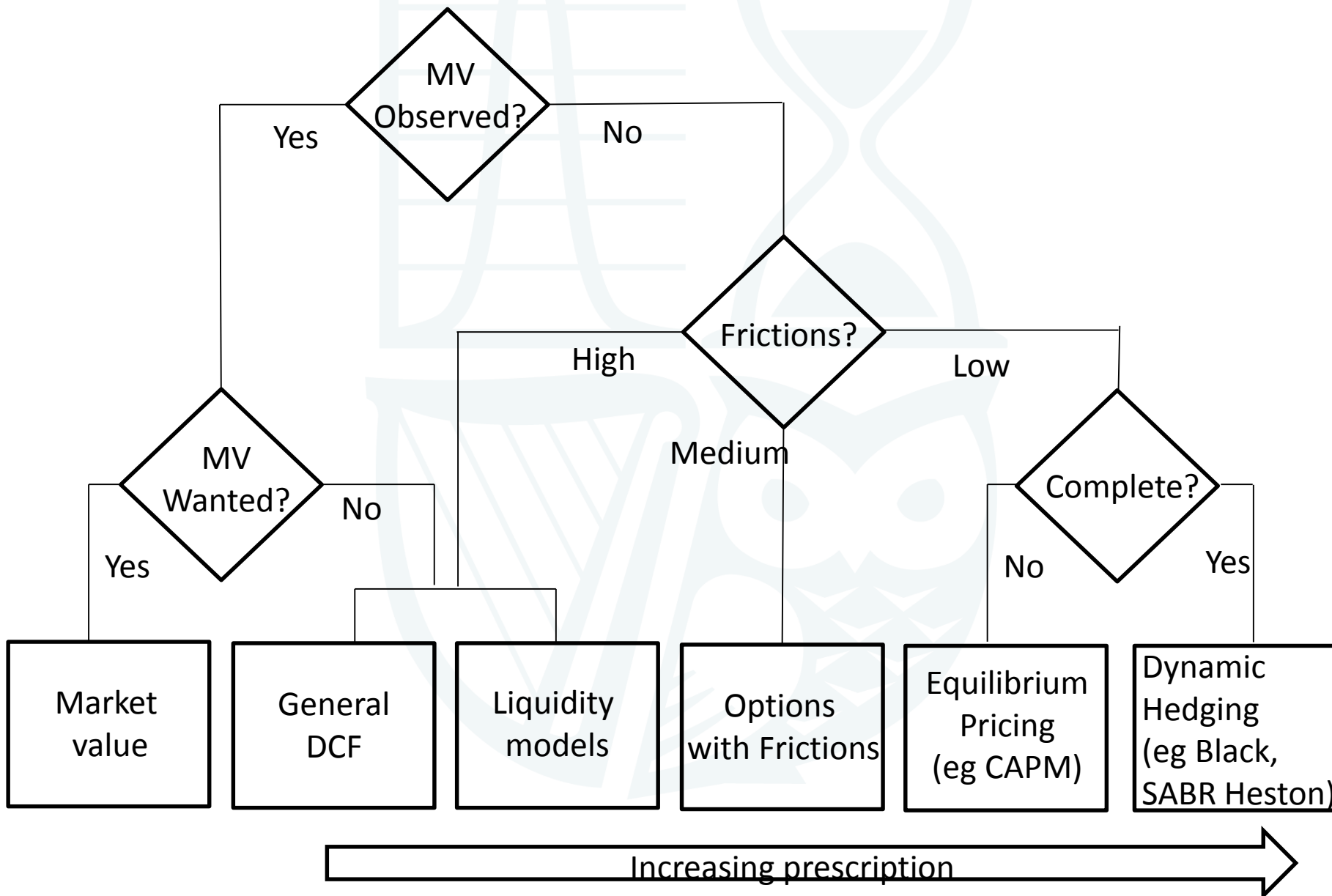
Historic and Projected House Prices



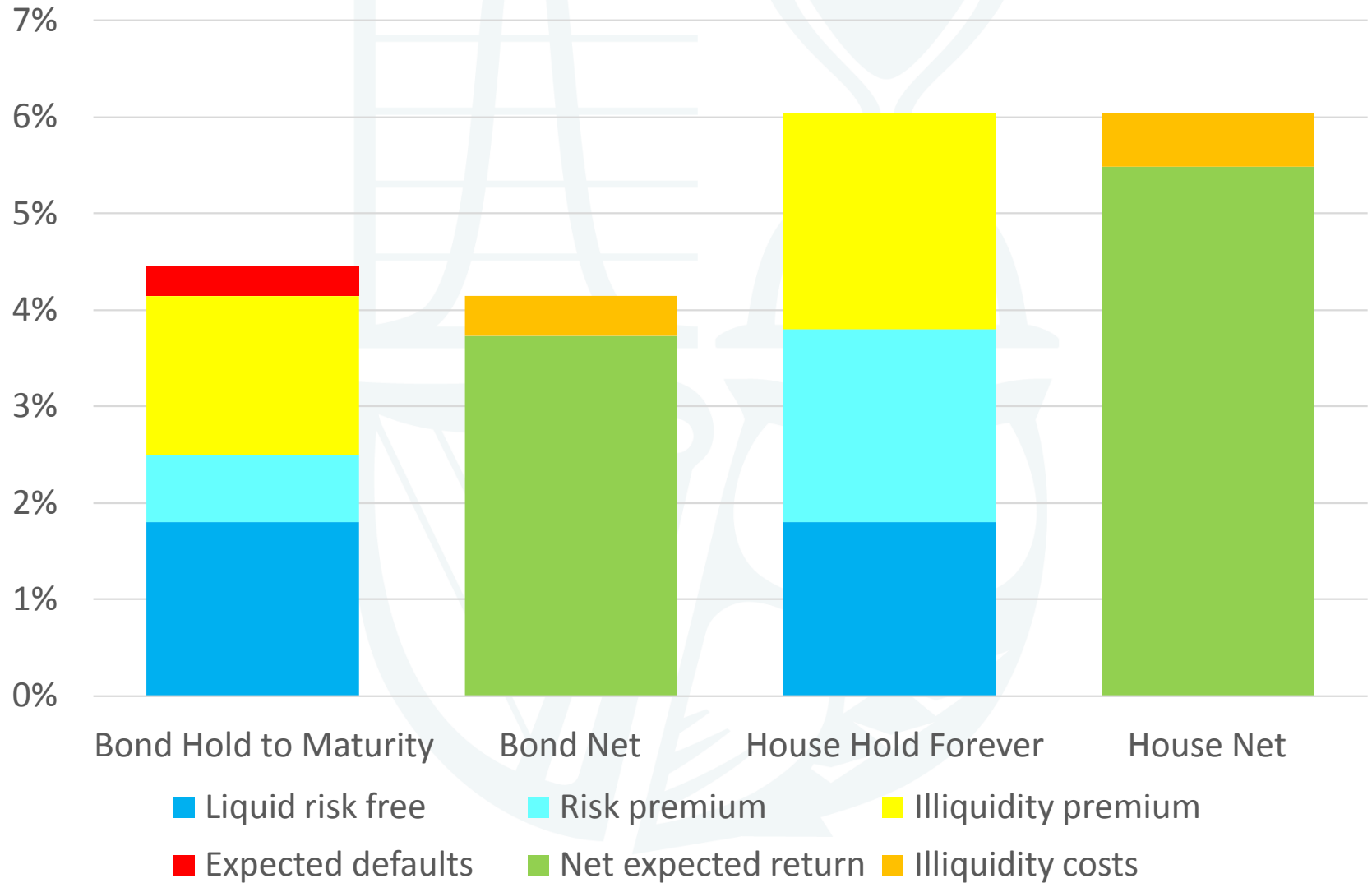
Historic House Index Volatility



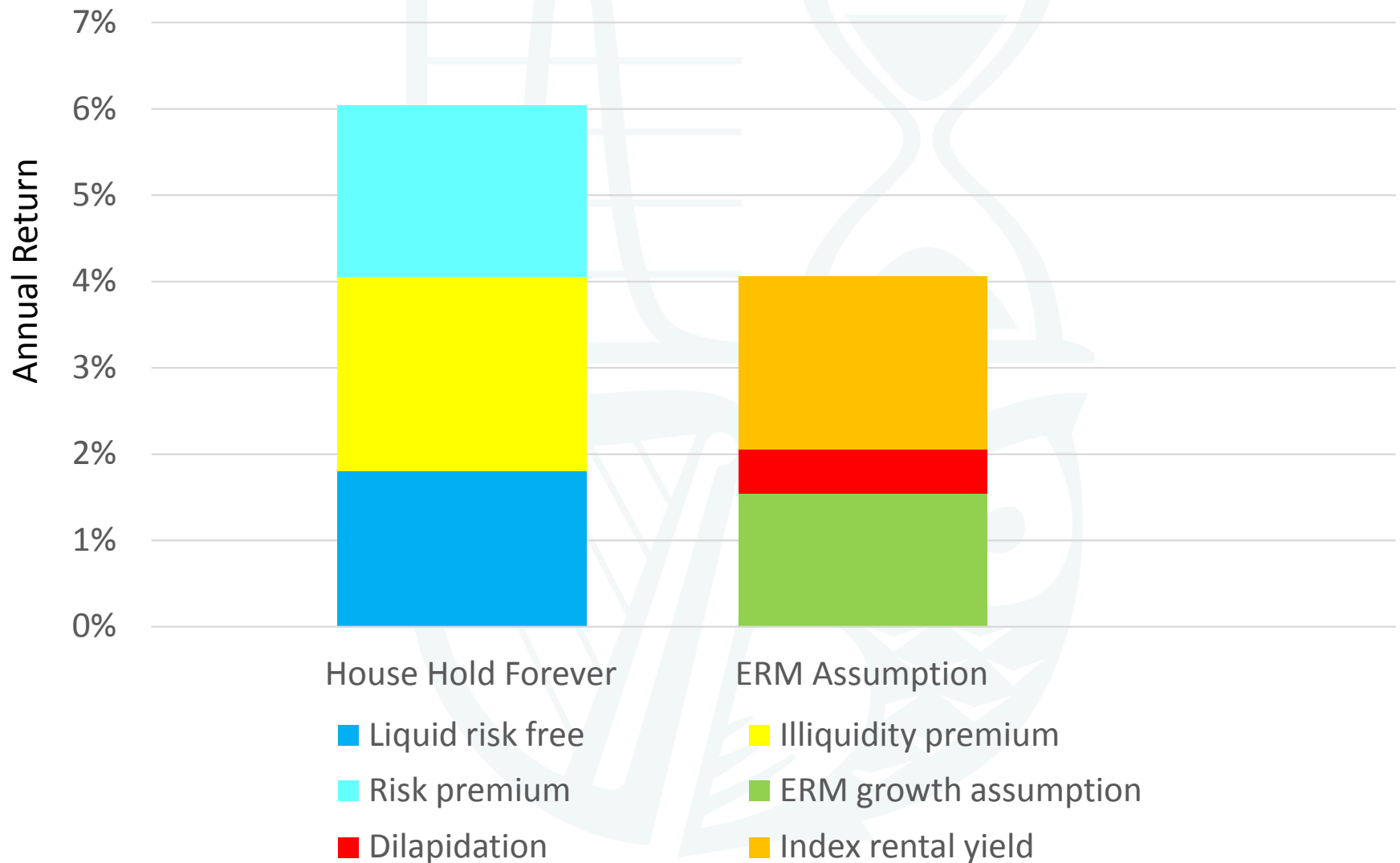
Fair Value Approaches: Many Possible Models



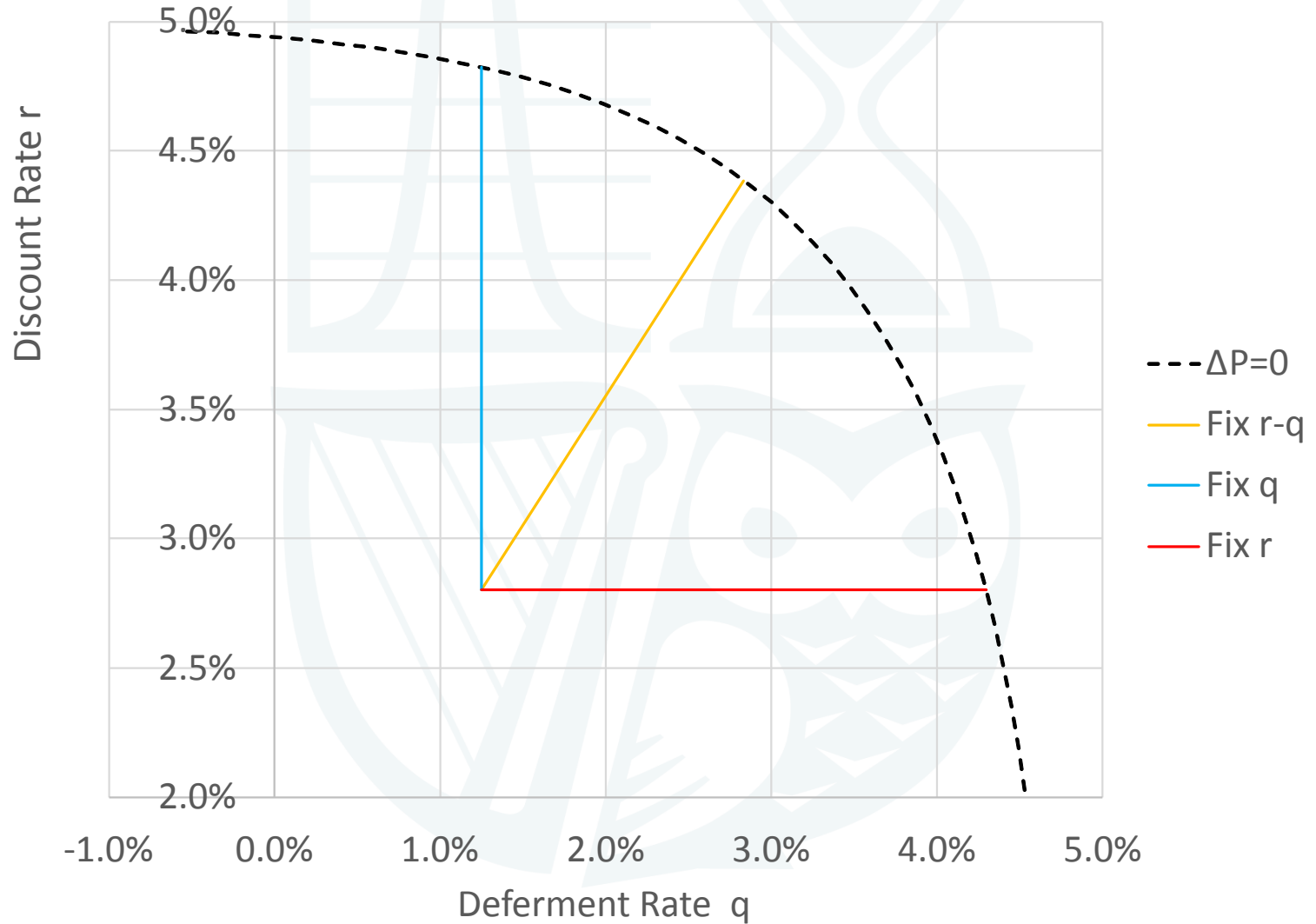
Returns on Bonds and on Houses



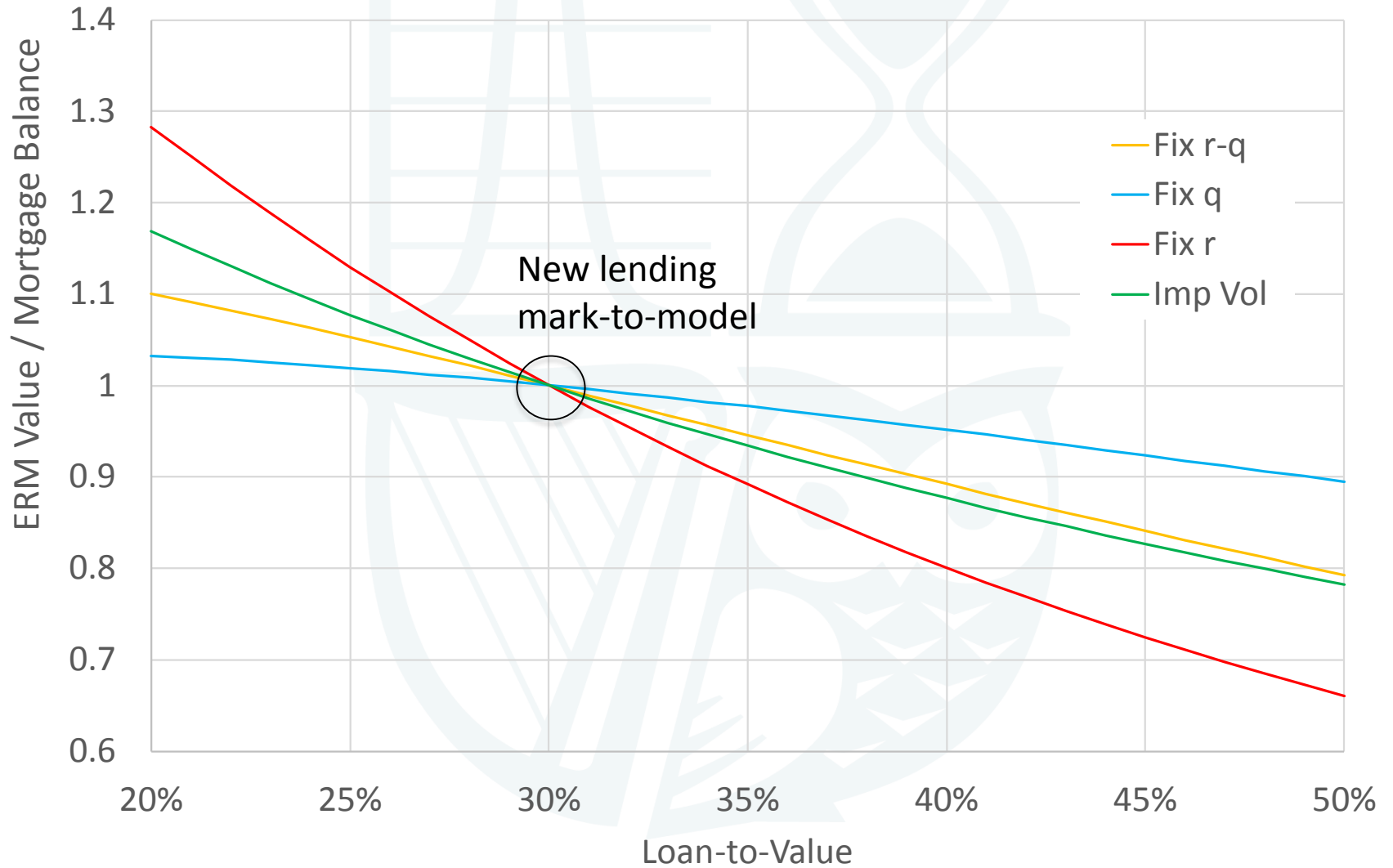
Illiquidity and House Growth Assumptions



Marking the Valuation Model to New Lending



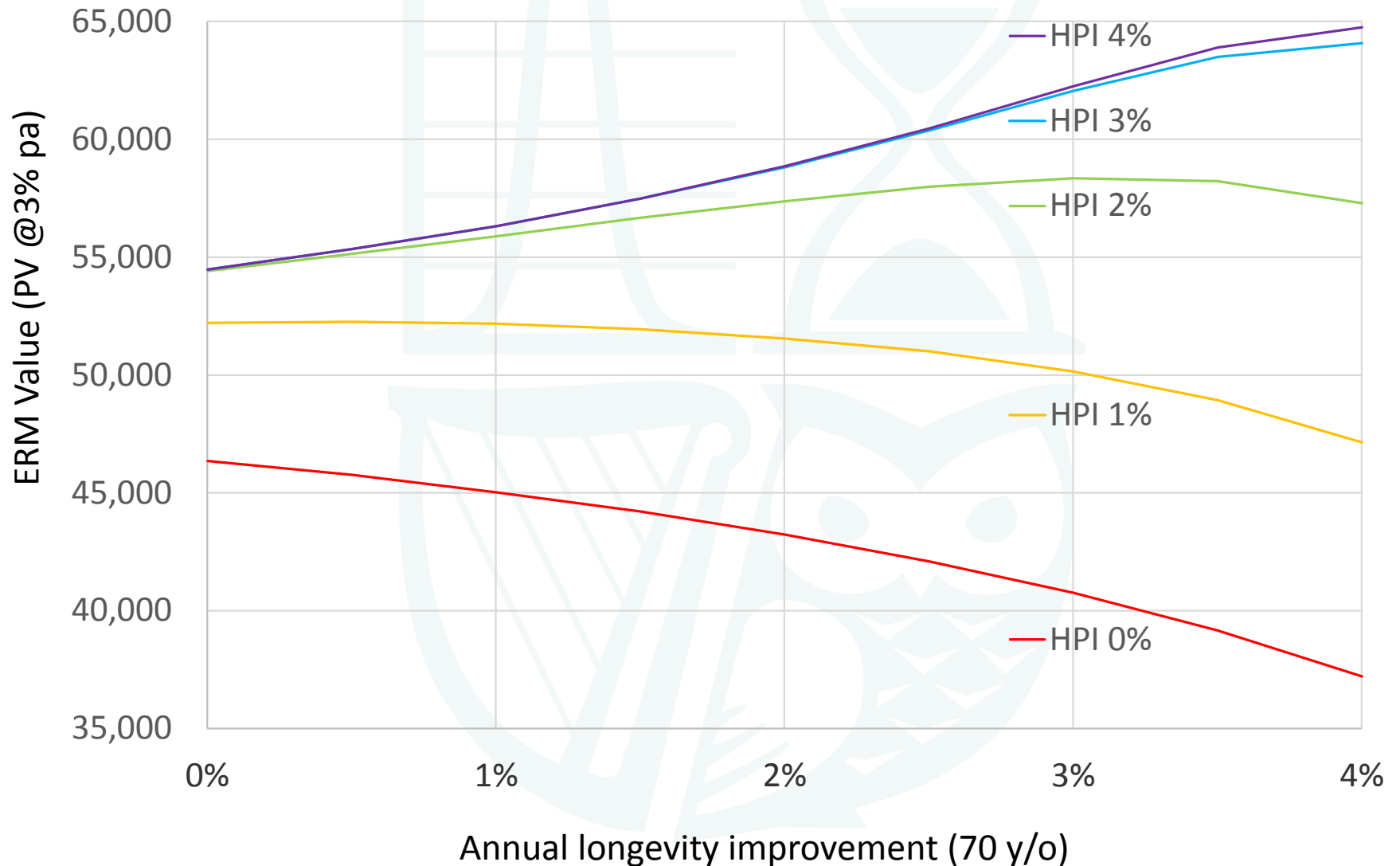
Loan-to-Value Sensitivity: Calibration Methods



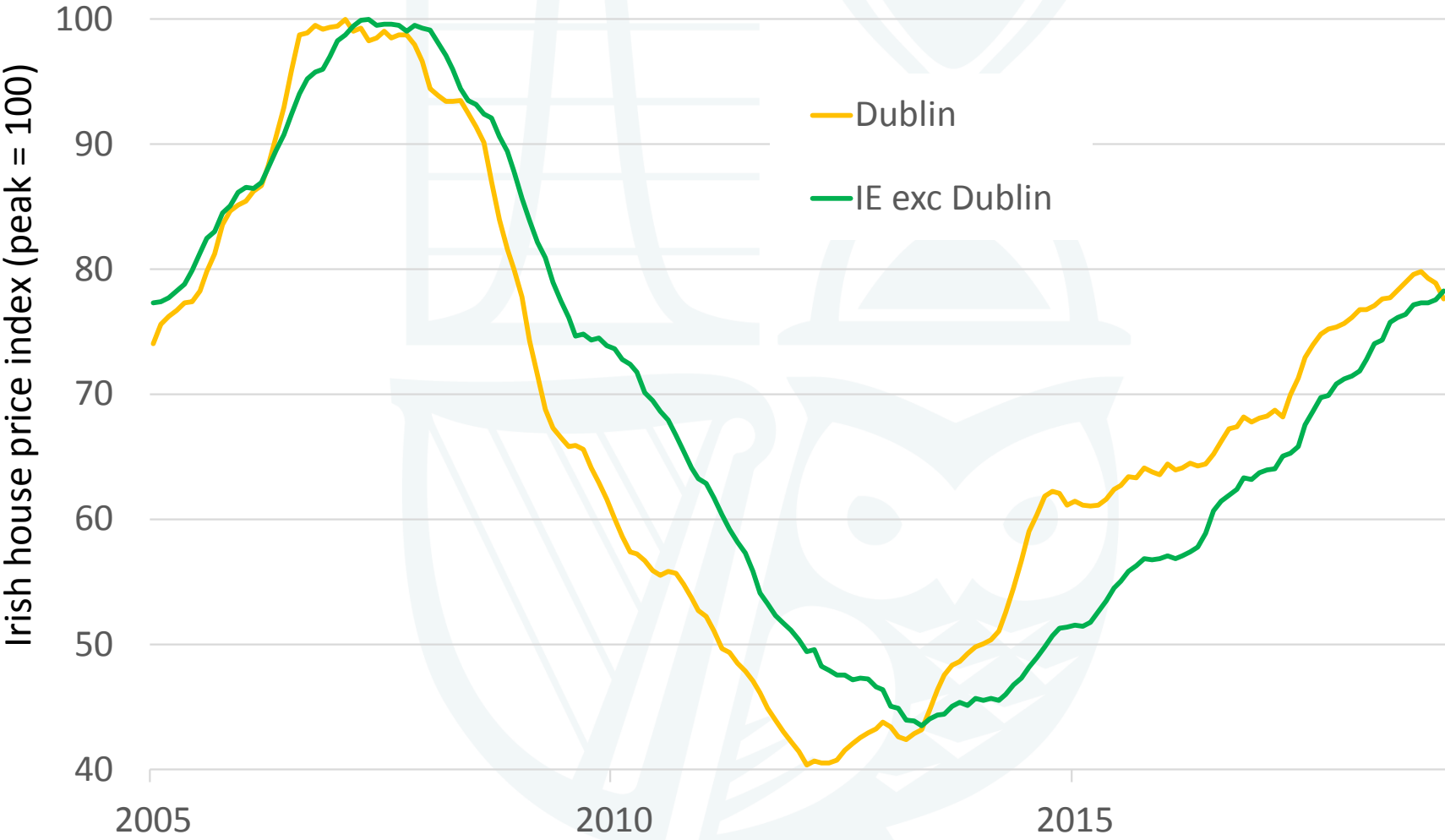
Are ERMs suitable for backing annuities?

- Yield
- Longevity hedge
- Liquidity
- Property risks
 - General
 - Specific
 - Dilapidation
- Macro-economics.

Do ERMVs hedge Annuity Longevity Risk?



Deriving Irish Residential Property Stresses



Should individuals downsize?

- Are geared investments really suitable for older people?
- Is down-sizing better?
- Are ERMs suitable for those who are either unable or unwilling to down-size?



Conclusions: Public Interest

- Cash flow for asset-rich, cash-poor.
- High yields may flow to higher individual and bulk annuity rates.
- Cash for home improvements and green retro-fits.
- Down-sizing eases house shortage.
- Best care not always in own home.
- Dilapidation; younger owners likely to invest.
- Insurers reliant on house price growth.



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