Summary
- Equity release is becoming more popular due to inadequate pension savings and innovation within the market.
- However, savers should not rely up on equity release alone to fund their retirement as usually it will not be enough.
- Experts agree that the two products, pensions and equity release, in the right circumstances, can complement each other to fund later life.

Good neighbours?

Equity release is on the rise, but what does this mean for the pensions industry? Natalie Tuck investigates

If you've ever spent some time on the sofa watching daytime television then you've most likely seen an all-singing, all-dancing advertisement for equity release.

The colourful adverts, often aired in the interval of the Aussie soap, *Neighbours*, offer viewers musical renditions on the benefits of equity release. Figures would suggest that the jolly tunes are hitting the right note; the Equity Release Council reveals that £3.94 billion of housing wealth was released in 2018, up 29 per cent year-on-year.

There are two main types of equity release products, a lifetime mortgage and a home reversion mortgage. With a lifetime mortgage the consumer takes out a mortgage on their house that they don't have to repay until they die, with the debt building up until that time. There is also a drawdown lifetime mortgage, which allows consumers to take money when they need it, offering more flexibility as consumers can usually pay some of the debt off while they are still alive.

The other type of equity-release product is a home reversion mortgage. In simple terms, this is when the company buys a proportion of the house from the consumer at an undercut price. For example, if a consumer had a house worth £100,000, and they sold a 40 per cent share to the provider, they might get £20,000 for that share; then when they die, the provider gets its 40 per cent stake back.

Gaining popularity

Key CEO, Will Hale, notes that a lack of pension savings and significant house price growth means that for many their house is their largest asset. The Equity Release Council's CEO Jim Boyd states that the Office for National Statistics' House Price Index (December 2018), shows the average house in the UK is worth £231,000, while the average pension pot is worth £105,496, according to Aegon (June 2018).

Therefore, Hale notes that as people contemplate longer retirements than previous generations "they are increasingly looking to equity release to fill the pension savings gap". The traditional way of freeing up cash in retirement may have been downsizing, but Hale says that many of the customers that Key speaks to want to remain in their current homes.

Alongside this, LEBC director of public policy, Kay Ingham, adds that wage growth has been muted for the past 10 years and this impacts on the pensions that people can expect to receive. This, she says, affects employer pension plans that are linked to earnings, either as a baseline for the percentage of contributions paid into a DC scheme or the percentage of final salary paid out from a DB scheme.

Equity release has also been boosted by significant investment and innovation within the market, More 2 Life CEO, Dave Harris, says. "Now customers can choose to make ongoing repayments, remortgage existing plans and include inheritance protection," he says. "This flexibility means that there are now more equity release products on the market than ever before, enabling advisers to find a product to meet each client's specific needs.

Risks

Despite its popularity, there is caution around equity release being the saviour of inadequate pension savings. Barnett Waddingham senior consultant, Malcolm McLean, notes that the commercials we see on television emphasise the positives and play down the negatives, including "high interest rate charges (normally between 6-7.5 per cent) and the way debt rolls up and can rapidly increase over time".

Recently on his ITV show, financial expert Martin Lewis warned consumers that it only takes around 14 years for what you owe to double (based on an interest rate of 5.1 per cent) due to the super compounding of interest.

Those who are looking for equity release to fill a gap in their pension savings may also be disappointed. A report last year by Royal London titled, *Will housing wealth solve the pensions crisis?*, found that wealth tied up in people's homes is no 'safety valve' for inadequate pension savings.

Using data from the W*ealth and Assets Survey* of around 7,000 pensioners across Britain, it found that the average amount of equity for poorer pensioners that do have property is around £150,000, compared to just over £400,000 for the richest fifth. For those that do have housing equity, equity-release providers will often only allow a pensioner to borrow around a third of the value of their property.

Most policies come with a 'no negative equity guarantee', and because of the impact of compound interest on equity-release loans through retirement, lenders want to make sure that the borrower retains significant equity at the

start of the policy. Therefore, at current annuity rates (August 2018), a pot of £50,000 (a third of a £150,000 property) could produce a weekly income of approximately £50 per week.

Therefore, Royal London director of policy, Steve Webb, says that equity release might be "more attractive as a way of topping up income (or paying for care) in later retirement, but you would need a lot of housing equity to fund a retirement if you can only access a third of it in retirement".

Boyd also notes that equity release should be seen as a supplement to pension income, as opposed to a substitute: "The government is right to focus considerable effort on encouraging consumers to save into pensions over the long term through initiatives such as auto-enrolment, alongside pensions tax relief."

Another risk, McLean notes, is that equity-release products could change in the future. "There is no absolute guarantee that equity release schemes will continue in the future exactly as they are now. Funding to support them may become less available, with the criteria for access much tighter, or they may become significantly more expensive."

Good neighbours become good friends?

With £136 of property wealth unlocked each second in the final quarter of 2018, it appears that equity release, for now, is here to stay. But if more consumers are choosing to fund their retirement with their home, will this hinder pension saving, or can good neighbours become good friends?

The idea that equity release can sit alongside pension savings as a way to fund later life is certainly gaining ground. Most recently, the government signalled its approval, backing the Housing, Communities and Local Government Select Committee's proposal that the Single Financial Guidance Body should signpost older people towards equity release as a home finance option.

This was in relation to older people freeing up cash to, for example, make modifications to their homes in readiness for later life. The Equity Release Council's chairman, David Burrowes, sees it as a "growing consensus that consumers will benefit by taking a more rounded approach to their retirement planning".

The Equity Release Council has also called for housing wealth to be included on the pensions dashboard, so people are better able to see how it can support them in retirement. However, that wasn't so well received by everyone, with Personal Investment Management and Financial Advice Association senior public policy adviser, Simon Harrington, tweeting that it is a "terrible idea".

There is no doubt though that experts from both industries agree that the two options of funding retirement can complement each other. McLean believes there is "room for both pensions and equity release". Webb notes that the two products could work together, "though the balance between the two may depend on individual circumstances".

On the equity release side, Harris says that from a customer perspective, equity release and pensions work well together, as people can use equity release to fill the gap left by pension under-saving. There are also benefits from a provider perspective, he says.

"Equity release books are often backed by annuities, as both of these products are long-term products and their customers have similar age profiles. As pension funds increasingly look for assets that match their liabilities, we anticipate that we will have more interest from investors with this types of capital."

Perhaps because of the overlap that Harris highlights, there are some providers that offer both pension and equity release products, with Just Group being one of them. Its communications director, Stephen Lowe, also notes that when a pension customer wants to use some or all of their pension pot to secure a guaranteed income for life, an insurance company has to invest their pension savings into a secure long-term investment.

"Insurance companies use some of that money to invest in lifetime mortgages; or put another way, they lend money to equity release customers. Both are long-term commitments."

Boyd states that there is a "natural synergy" between the products, for both providers and consumers. So perhaps, the two really are the perfect blend.

Written by Natalie Tuck