

# **ASSET DEPLETION AND CASH FLOW INCREASE EFFECTS OF REVERSE MORTGAGE USE BY ELDERLY HOUSEHOLDS**

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Use of a reverse mortgage (RAM) by an elderly household will increase cash flow while using up a major asset. Capital market imperfections and regulatory, economic, and demographic conditions have impeded development of home equity conversion instruments in the past. Current incentives for development are changes in capital markets and pilot project successes. Quantitative analysis focused on elderly households from the Longitudinal Retirement History Study. A simple rising balance RAM loan was simulated based on value of the home. RAM payments resulted in median real cash flow increases of 11 to 18 percent during the ten year analysis period. Between 25 and 35 percent of poverty households moved above the line with use of a RAM.

Median real net worth increased 33 percent over the decade, enough to offset depletion of net home equity due to RAM use. Fifty-one percent of respondents ended the decade with higher net worth, even with RAM use. For 12 percent, net worth decreased if a RAM was simulated. Separate analysis of low-income households showed even greater cash flow increments (17 to 23 percent) and comparable net worth changes. For 14 percent, net worth decreased with a RAM; 43 percent had higher net worth at the end, even with RAM use.

The effect of RAM use by public assistance recipients was analyzed by assuming several patterns for offsets against benefits. Treating RAM payments as earned income was the only offset format which allowed significant improvement in cash flow. Because of low home value,

the benefits for this group are too low to justify the widespread use of RAMs by public assistance recipients.

Asset depletion results differed according to the time period selected. Appreciation was greater than depletion only when a longer term was selected. Homeowners should be helped to an understanding of asset depletion risk when shorter term loans are used.