

Base Rate Drops to 1.5% But How Effective Will it Be?



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Today's decision to reduce the base rate by 0.5% to an all time low of 1.5% was widely anticipated but base rate cuts alone are no longer an effective economic tool.

The direct impact of base rate cuts felt by borrowers is limited by lenders' collared tracker products and their unwillingness to pass on the lower rates in SVRs. This is seen particularly from lenders that are not government funded. However, today's fall does offer a degree of reassurance and stability.

Neil Young, CEO of property portfolio managers, Young Group, believes that with rates so low, and with little scope to fall further, lenders now have more certainty; *"with rates reaching a new low, there is a limit as to how much further they can fall. This enables lenders to increase the confidence of their forecasts when planning product for the year ahead and should lead to an increase in their willingness to lend.*

"This first MPC decision of 2009 is akin to the Bank of England giving its opening team talk of the season. Base rate is unlikely to fall much further, lenders know what's expected of them and the onus is now on them to go out there and perform."

In the current climate, base rate setting is no longer the economic tool that it once was and is becoming less effective the lower rates fall. Building societies are facing increasing difficulties; balancing being able to offer competitive rates to retain their savers with offering their mortgage lending to their borrower; yet another reason why rates are not being passed on to borrowers. Base rate cuts alone are not the solution.

Borrowers are increasingly savvy regarding the impact of base rate cuts and their focus is on availability of lending rather than base rate. The latest Young Index poll (Q4 2008) has identified that only 12% of respondents expressed a desire for a lower base rate, whereas 28% put the need for wider mortgage choice at the top of their wish list.