

5 February 2009

The Bank of England's 0.5% Base Rate Reduction Will Not Increase Liquidity, Nor Help Savers

It was widely predicted that the UK's Bank of England Monetary Policy Committee (MPC) would announce a further cut in base rate following February's rate setting deliberations. In line with consensus predictions, the rate has been reduced by 50 basis points, bringing the base rate down to a new all time low of just 1%.

Neil Young, CEO – Young Group, is concerned that this month's cut in the UK's base rate will not have the impact that the Bank of England hopes. "The further cut in base rate will benefit those lucky enough to be on tracker mortgages and some on standard variable rates if the lenders opt to reduce their rates, but in total that's only around 35 per cent of mortgage holders."

Up to 65 per cent of borrowers will see no benefit from the Monetary Policy Committee's (MPC) decision and are not in a position to change their mortgage for a more favourable product due to lenders' restrictive lending criteria.

"The economy is crying out for liquidity but successive cuts in base rate have not made an appreciable impact on lenders' willingness to provide credit. Whether purchasers and homeowners are looking for mortgages or businesses are seeking funding, lenders are still placing restrictive hurdles in their path," continued Young.

Lenders are coming under increasing pressure to lend as a result of the increase in margins brought about by interest rate cuts and further falls in base rate will only increase calls for them to free-up their lending. But, arguably, lenders are in need of increased margins to cover the effect of previous toxic lending. Until they are back on a more even footing, or forced by the treasury to increase liquidity by relaxing their lending criteria, base rate cuts will not mean wider mortgage choice for borrowers or easier access to finance for businesses.

Meanwhile, much press attention has been given to savers who are seeing the interest generated by their deposits dwindle in the face of falling savings rates. But commenting on the issue, Neil Young points out, "The alternatives to saving – which is generating little return due to low interest rates – are to spend or to invest, both of which provide economic stimulus and could aid the wider economy."