Base rate cuts could limit loans and mortgages

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Responding to a new survey suggesting that two thirds of people are opposed to the recent base rate cut due to the pressure on banks to lower interest rates on savings accounts, financial solutions company Think Money has warned that lenders' ability to offer loans and mortgages could be limited if the base rate continues to fall.

The survey, carried out by Moneysupermarket.com, showed that over two thirds (67%) opposed the most recent Bank of England base rate cut. 42.8% of respondents opposed the cut because their income would fall again due to savings losses, while 24.4% were fixed-rate mortgage (http://www.thinkmoney.com/mortgage/) holders whose monthly payments would be unaffected.

Indeed, several analysts – including the BBC's Business Editor Robert Peston – had previously suggested that base rate cuts are not the best way of tackling the economic crisis.

A mortgage & loans (http://www.thinkmoney.com/loans/) expert for Think Money commented: "Base rate cuts are partly aimed at reducing the wholesale cost of funding, therefore making loans and mortgages cheaper to both the lender and the borrower.

"However, the base rate has become so low that lenders' savings rates are beginning to suffer. When the base rate falls, so do interest rates on savings accounts. This could discourage increasing numbers of people from putting their money into savings, which limits the cash flow into banks, and this further limits their capacity to offer loans and mortgages."

The spokesperson added that the base rate cuts have not had the desired effect in many cases. "So far, we have only seen significant interest rate cuts on mortgages. Rates on personal loans have remained relatively unchanged.

"Looking at the wider picture, we have a situation in which borrowing has not become much cheaper in some cases, but there is much less incentive to save – which is why economists are calling for other measures to help the financial crisis."

However, the Think Money spokesperson was keen to mention that the long-term prospects of lower rates on both loans and mortgages is good, so long as the base rate remains low. "There are other factors that are currently affecting lender's willingness and ability to offer loans. The LIBOR rate is still above the base rate, as banks are still fairly cautious about lending to each other, meaning the funds needed for loans and mortgages are expensive.

"But in the future, if banks become more confident about their lending, it's very much possible that we will begin to see reduced interest rates on both loans and mortgages.

"The housing market slump is expected to continue well into 2009, while many economists are expecting a period of deflation this year, so it's unlikely the base rate will rise in the next few months. All that's needed is an increase in the funding available to lenders and we could see more loans and mortgages being offered."

The spokesperson also emphasised the importance of good advice when it comes to finding loans or mortgages. "We advise anyone looking for a loan (http://www.thinkmoney.com/) or mortgage to speak to an expert. Not only can they advise people on the best course of action for their circumstances, but they can also take the effort out of finding the best deals – which is becoming more important in the difficult loans market."

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Think Money work with a panel of lenders to offer a range of loans and mortgages. If you are considering taking out a loan or looking for mortgage advice (http://www.thinkmoney.com/), contact one of our expert mortgage advisers today.

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