



THE BANK OF ENGLAND -

Holding their nerve or losing the plot? *By Doug Cowan*

Yet again the Bank of England has held the base rate at 0.5%, leading to many questions as to the impact of this decision on a slow but fragile economic recovery and the ever rising cost of living (inflation). What is certain is that this low base rate is forcing mortgage lenders to review their product range and to be more competitive in their pricing, especially when it comes to fixed rate products. The current market view is that the low base rate is likely to be with us until the last quarter of 2011 or maybe into early 2012, but who knows? What we can be sure of is that when rates do begin to rise, so will all of the products currently on offer.



There are many arguments from both sides as to why interest rates should remain low or why they should be increased. What is agreed is that the interest rate is unlikely to reduce, so what does this mean for the mortgage customer? I think it is fair to say that many mortgage holders have

found themselves over the last 2 years on low standard variable rates with no motivation to consider alternatives. If it is accepted that rates will only rise, consideration should be given to taking advantage of lower rates now in order to benefit over the longer term.



2 and 3 year fixed rates at record lows

Short-to-medium term fixed rate deals have hit their lowest ever level, according to Moneyfacts. This could be the spur to borrowers to consider re-mortgaging now.

The average two-year fixed rate in the UK in June 2011 was 4.36%, with the average three year rate at the lowest on record at 4.95%.

A fall in fixed mortgage rates is great news for borrowers who have wrestled with high fixed rates for many months. Lenders appear to be launching more competitive deals and expanding their product ranges, with lower rates and higher loan-to-value deals, however, strict lending criteria and thorough credit checks do remain in place.

Fixed rates are hitting record lows because the general view is increasingly that the base rate won't change until 2012. So this could represent good value for money in the longer term for those securing a fixed rate now.

5 year fixed rates below 4%

The average five year rate, at 5.37%, is at its lowest since January 2011.

Currently, there are just three five-year deals on offer under 4%, including Chelsea Building Society with the lowest five-year fix at 3.89%, Yorkshire Building Society offering 3.99% and The Mortgage Works also offering 3.99%, with a 2% fee. When you consider that the Bank of England base rate was 5.5% in June 2008 with fixed products on average at 6.75% this makes the current fixed products very attractive indeed.

As far as fixed-rate mortgages are concerned, an important psychological barrier is broken whenever a five-year fixed rate edges below 4%. Historically, this is an extremely low rate and a welcome tonic to the borrower looking for certainty for a number of years at a rock-bottom price. If lenders feel able to offer pricing at that level, then the markets clearly don't think interest rates are going to rise any time soon.

Mortgage rates can also come down when lenders want to pick up more business. The middle of the year is a good time for this to happen as lenders look at their lending book and see where they are now, compared with where they wanted to be by the middle of the year. If they haven't done enough lending to stay on track then now is the time for a few cut-price offers.

But the interest rate environment is the real issue at the moment. The International Monetary Fund (IMF) recently complimented the Chancellor on his deficit cutting approach and said that he should carry on with more of the same. Inflation is expected to fall on the back of this and, if it does, the IMF concludes that interest rates won't need to rise for some time. This has led many to assume that this means 2012 at the earliest, and the markets have responded with lower borrowing rates.

4%

What does this mean for the borrower?

Borrowers who have been waiting for really cheap five-year fixed rate deals and have the necessary equity in their home or sufficient deposit to qualify for the best deals should now be able to find what they are looking for.

Those who don't need the certainty of a fixed rate can also find bargains, with trackers falling to low levels.

This means that some Tracker rates are even better than the cheapest standard variable rates and, if interest rates aren't going to rise in the near future, this may make perfect sense for some.

Conclusion

For the last couple of years it has been best practice for mortgage customers to sit on standard variable rate mortgages as typically this was cheaper than most alternatives on offer. This is clearly no longer the case and in fact with the lowest rates in history on offer, it is only a matter of time before interest rates increase again. It is all about timing and a bit about playing the market, but taking no action can prove to be costly.

To take advantage of today's low rates independent financial advice should be sought in order to ensure that any mortgage is appropriate to the client's individual requirements.

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