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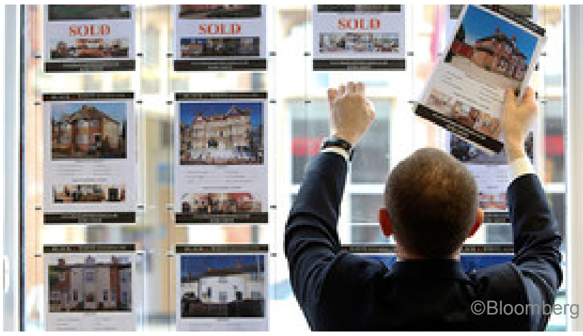
Funding for Lending scheme likely to keep UK mortgage rates low

By Tanya Powley



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Mortgage rates for homeowners and landlords are likely to remain low over the next two years as the Bank of England this week revealed plans to extend its Funding for Lending scheme (FLS) to the start of 2015.

On Wednesday, the BoE announced a package of reforms that will see the scheme run for longer as well as increasing the number of incentives available to banks to lend to small businesses.

The FLS, which offers lenders cheaper funding than that available in financial markets in return for increased lending to households and companies, has already helped lower mortgage rates since its launch in August.

The average five-year fixed-rate repayment loan rate has fallen from 4.73 per cent in August to 3.97 per cent today, according to figures from Moneyfacts, the financial data provider.

It has also helped bring down the cost of borrowing for buy-to-let landlords, with the average variable rate down from 5.09 per cent to 4.28 per cent today, leading some to dub it the "Funding for Landlords" scheme.

"The positive effect on mortgage pricing since the FLS was introduced has been obvious," said Mark Harris of mortgage broker SPF Private Clients.

Two-year fixed-rates for borrowers with deposits – or equity – of 40 per cent or more are now as low as 1.74 per cent from Chelsea Building Society. Borrowers can also fix their mortgage for five years at 2.59 per cent from Yorkshire Building Society.

How Funding For Lending has affected mortgages and savings

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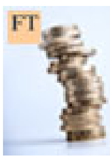
On Friday, Yorkshire Building Society also launched a 10-year fix at 3.99 per cent for homeowners with deposits – or equity – of 25 per cent or more. It comes with no product fee.

The number of mortgage products across different loan-to-value bands has also increased in recent months. For example, the number of 80 per cent loan-to-value mortgages has risen from 397 in August to 560 today.



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However, while mortgage rates have fallen and the choice of products has risen, the scheme has had less impact on increasing the volume of lending. Net lending contracted by £2.4bn in the fourth quarter of 2012, according to BoE figures published last month. This was the first period when any meaningful improvement due to FLS would have been seen.

Recent figures from the Council of Mortgage Lenders revealed that gross lending in the first quarter of 2013 was an estimated £33.8bn – down 9 per cent from the last quarter of 2012 and virtually unchanged from the first quarter of 2012.

“Funding for Lending has produced cheaper mortgages but it has had limited success in widening access to mortgages as lending criteria remains tight,” said Nigel Bedford of Largemortgageloans, the mortgage broker.

However, experts believe there are signs that this is changing. According to Ben Thompson of Legal & General Mortgage Club, some building societies are launching products targeted at more niche markets, such as first-time buyers and self-employed borrowers.

For example, Saffron Building Society recently launched a 95 per cent mortgage that does not require any additional money – or guarantees – from parents.

Thompson believes the next set of quarterly lending data from the Bank of England, to be unveiled on June 3, could show a more positive impact. “We’ve had a very good April, so this should show in figures for May and June. There are a lot of encouraging signs, such as the recent rise in first-time buyer activity,” he said.

However, some experts, such as Capital Economics, warn that the Bank of England’s new focus on encouraging lending to small businesses could see banks lend less to homeowners.

One group of consumers unlikely to be happy by the extension of the FLS is savers. Savings rates have plummeted to all time lows since the introduction of the scheme, eroding the amount of income earnt by savers.

For example, the average two-year fixed rate bond has fallen from 3.29 per cent in August to 2.07 per cent today. Interest rates for the average no-notice account have dropped from 1.09 per cent to 0.76 per cent today.

“It seems no savings accounts are left untouched by this recent trend, with many providers no longer needing savers to balance their mortgage book,” said Charlotte Nelson of Moneyfacts.

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