Age-old complaint about savings rates is down to you rather than bank bosses

The bosses of Britain's leading commercial banks – Barclays, NatWest, HSBC and Lloyds Banking Group – appear before the Treasury select committee of MPs on Tuesday.

They face questions on a range of issues including branch closures, the mortgage market and the government's proposed reforms to financial regulation that were unveiled just before Christmas.

Potentially the stickiest questions they face, though, will be on the question of whether they are passing on to savers the increases in interest rates made over the past 14 months by the Bank of England – taking Bank Rate, its policy rate, from the record low of 0.1% to 4% as of last Thursday.

As the Committee noted: "Customers of Barclays, HSBC, Lloyds Banking Group and NatWest Group can expect to earn between 0.5% and 0.65% interest on basic savings accounts.

"MPs on the cross-party committee will ask why these rates are so low, and whether banks can be doing more to advise customers on how to arrange their funds to maximise the return they receive."

The committee has, apparently, been motivated by a deluge of complaints to politicians from constituents that the banks have not been passing on the benefits of higher interest rates to savers.

Those complaints, according to the independent research, monitoring and price comparison service Moneyfacts, appear justified.

It noted last week that, while interest rates on variable savings accounts had risen and that several providers had “improved their offers since the start of 2023”, the best savings rates were being offered by the challenger banks and building societies rather than by the established commercial banks.

Moneyfacts added: “Savers who fail to review their existing account to the latest top rates may miss out.

“Loyalty does not always pay, and the majority of the biggest high street banks have failed to pass every Bank of England base rate rise to easy access accounts, with two brands passing on just 0.54% since December 2021.”

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BoE governor explains interest rate rise

Before the latest increase from the Bank of England, on Thursday last week, Moneyfacts published figures suggesting the average easy access savings account was paying an interest rate of 1.54% – up from 0.2% at the beginning of December 2021. During the same period, Bank rate rose from 0.1% to 3.5%.

So why the inertia? The first point to make is that the banks are under no obligation to pass on the full extent of increases in Bank rate to savers.

Near-zero interest rates of the kind the UK had from 2009 to 2021 had a crushing impact on net interest margins – the spread between what borrowers are charged and depositors are paid – and so the banks will be looking to rebuild profits after a decade in which they have been under intense pressure.

A second key factor is that the banks also know a lot of their customers do not trust some of the challenger banks offering more competitive rates and, accordingly, trade off that inertia.

Savers are, in effect, paying a safety premium for keeping their money with a trusted name like Barclays or NatWest than with a bank of which they may never have heard.

That, incidentally, is completely rational. Many will recall how, during the financial crisis, savers who had opened deposit accounts with the little-known Icesave, attracted by its market-beating rates, faced months of uncertainty when it collapsed in 2008.

In addition, many of the best savings rates are to be found with online-only providers, who often require savers to have a smartphone app. That may not suit some older or less tech-savvy savers.

Some politicians highlight the way that the banks have been quick to pass on the increases in Bank rate to mortgage customers.

Why, they ask, do the banks not pass on those increases to savers in the same way? The answer is because there is no link between the savings market and the mortgage market. The pricing of both is down to individual banks based on conditions in the market. And it is a fact that mortgage borrowers are more inclined to shop around in search of a better rate than savers are.

Image:
There is no link between savings rates and mortgage rates
Another factor to bear in mind is that the banks do not exactly have to rush to raise money from depositors at present.

The banks have plenty of ‘liquidity’ at the moment – in other words they have plenty of ability to meet their financial obligations, as they fall due, via cash holdings or other instruments, such as short-dated bonds. They simply do not need to chase deposits.

It is also worth noting that this is not just a UK phenomenon.

The European Central Bank began raising interest rates in July last year and, with its latest hike coming last Thursday, it has taken rates from -0.5% to 2.5%.

Not all lenders in the eurozone have been passing on those increases to customers and there has been particular unhappiness in Spain, where as of December, average returns on one year deposits stood at 0.42% against a eurozone average of 1.34%.

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Further afield, Australia's finance minister has just indicated he will be instructing the country's competition watchdog to investigate the savings account market, where again rates have not kept up with the official rate.

From May to December last year, the Reserve Bank of Australia took its main policy rate from 0.1% to 3.1%, a 3 percentage point increase. The average savings rate has risen by just 1.82 percentage points in that time.

Unhappiness at the refusal of deposit-takers to pass onto savers the full extent of interest rate rises is not new. In 1998, the then-Chancellor, Gordon Brown, commissioned Don Cruickshank, the former telecoms regulator, to carry out a review of banking services in the UK.

Mr Cruickshank's report, when it was published in March 2000, concluded that UK banking customers – both personal and business – were overpaying by between £3-£5bn per year and, for personal customers, he identified three product areas – credit cards, savings accounts and personal loans – as being particularly problematic.

His report did, undoubtedly, lead to some improvements. It became far easier to switch current accounts while the speed at which money is transferred from one account to another increased dramatically.

Yet the complaints made today about savings rates remain similar to the ones made 25 years ago.

Mr Cruickshank uncovered, during the course of his research, that the average person keeps the same savings account for almost 10 years – while only 18% of savers knew exactly what rate of interest they were receiving.

It seems little has changed in terms of customer inertia and, until it does, that minority of savers who actually do know how much interest they are receiving are likely to carry on feeling badly done by.