Appendix C

Arlingclose Economic Outlook & Interest Rate Forecast

Interest rate forecast:

- The MPC remains concerned about inflation but sees the path for Bank Rate to be below that priced into markets.
- Following the exceptional 75bp rise in November, Arlingclose believes the MPC will slow the rate of increase at the next few meetings. Arlingclose now expects Bank Rate to peak at 4.25%, with a further 50bp rise in December and smaller rises in 2023.
- The UK economy likely entered into recession in Q3, which will continue for some time. Once inflation has fallen from the peak, the MPC will cut Bank Rate.
- Arlingclose expects gilt yields to remain broadly steady despite the MPC's attempt
 to push down on interest rate expectations. Without a weakening in the inflation
 outlook, investors will price in higher inflation expectations given signs of a softer
 monetary policy stance.
- Gilt yields face pressures to both sides from hawkish US/EZ central bank policy on one hand, to the weak global economic outlook on the other. BoE bond sales will maintain yields at a higher level than would otherwise be the case.

	Current	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25
Official Bank Rate													
Upside risk	0.00	0.25	0.50	0.75	1.00	1.00	1.00	1.25	1.50	1.75	1.50	1.25	1.25
Arlingclose Central Case	3.00	3.50	4.00	4.25	4.25	4.25	4.25	4.00	3.75	3.50	3.50	3.50	3.50
Downside risk	0.00	0.25	0.50	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00
3-month money market rate													
Upside risk	0.00	0.25	0.50	0.75	1.00	1.00	1.00	1.25	1.50	1.75	1.50	1.25	1.25
Arlingclose Central Case	3.00	3.90	4.40	4.40	4.40	4.35	4.30	4.25	4.00	3.75	3.75	3.75	3.75
Downside risk	0.00	0.25	0.50	0.75	0.75	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00
5yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.36	3.65	3.90	3.90	3.90	3.90	3.80	3.70	3.60	3.50	3.40	3.30	3.20
Downside risk	0.00	0.70	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
10yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.46	3.70	3.75	3.75	3.75	3.70	3.70	3.70	3.70	3.70	3.70	3.70	3.70
Downside risk	0.00	0.70	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
20yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.88	4.00	4.00	4.00	4.00	4.00	3.90	3.90	3.90	3.90	3.90	3.90	3.90
Downside risk	0.00	0.70	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
50yr gilt yield													
Upside risk	0.00	0.60	0.70	0.80	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Arlingclose Central Case	3.24	3.40	3.40	3.40	3.40	3.40	3.30	3.30	3.30	3.30	3.30	3.30	3.30
Downside risk	0.00	0.70	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00

Underlying assumptions:

- UK interest rate expectations have eased following the Autumn Statement, with a
 growing expectation that UK fiscal policy will now be tightened to restore investor
 confidence, adding to the pressure on household finances. The peak for UK
 interest rates will therefore be lower, although the path for interest rates and gilt
 yields remains highly uncertain.
- Globally, economic growth is slowing as inflation and tighter monetary policy depress activity. Inflation, however, continues to run hot, raising expectations that policymakers, particularly in the US, will err on the side of caution, continue to increase rates and tighten economies into recession.
- The new Chancellor dismantled the mini-budget, calming bond markets and broadly removing the premium evident since the first Tory leadership election.
 Support for retail energy bills will be less generous, causing a lower but more prolonged peak in inflation. This will have ramifications for both growth and inflation expectations.
- The UK economy is already experiencing recessionary conditions, with business activity and household spending falling. Tighter monetary and fiscal policy, alongside high inflation will bear down on household disposable income. The shortto medium-term outlook for the UK economy is bleak, with the BoE projecting a protracted recession.
- Demand for labour remains strong, although there are some signs of easing. The
 decline in the active workforce has fed through into higher wage growth, which
 could prolong higher inflation. The development of the UK labour market will be a
 key influence on MPC decisions. It is difficult to see labour market strength
 remaining given the current economic outlook.
- Global bond yields have steadied somewhat as attention turns towards a possible turning point in US monetary policy. Stubborn US inflation and strong labour markets mean that the Federal Reserve remains hawkish, creating inflationary risks for other central banks breaking ranks.
- However, in a departure from Fed and ECB policy, in November the BoE attempted
 to explicitly talk down interest rate expectations, underlining the damage current
 market expectations will do to the UK economy, and the probable resulting inflation
 undershoot in the medium term. This did not stop the Governor affirming that there
 will be further rises in Bank Rate.