BANK RATE RISES TO 15-YEAR HIGH, FURTHER HIKES ANTICIPATED

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The Bank of England's (BoE) Monetary Policy Committee (MPC) raised interest rates by 0.25% to 5.25% on Thursday 3rd August, as expected by most economists.

The decision was approved by a majority of six to three, with two members supporting a 0.5% increase and one member preferring to maintain the rate at 5%. The MPC have emphasised that the current hiking cycle is data dependent and further tightening could be necessary until inflation is brought closer to the 2% target. This is the 14th consecutive hike to the base rate, which has risen from 0.1% in December 2021, and is the highest rate in 15 years. Although inflation declined in June, the market is still pricing in a further two hikes from the BoE, with another 25bps-hike this year and a projected terminal rate of 5.75% in Q1 2024.

The latest UK inflation data for the twelve months to June was 7.9%, down from 8.7% in May and October 2022's peak of 11.1%. Despite being on a downward trajectory however, inflation is still falling at a far slower rate than anticipated. Core goods and services inflation both came in lower than expected, although the primary contributors to the reduction were falling fuel prices, gas and electricity bills. Wholesale gas and energy prices have fallen significantly with Ofgem reducing the price cap from the 1st July and, based on futures gas prices, another reduction is anticipated in October. In the MPC's latest Market Participants Survey, predictions are that inflation will decline to around 5% by the end of the year and just over 2% by Q3 2025.

UK GDP for Q2 of this year is expected to be moderately stronger than previously predicted, following a slightly weaker than anticipated Q1 result, with current estimates anticipating growth of 0.1%. Taking a broader view, growth is predicted to increase to around 0.4% in 2023, 15bps stronger than thought in the previous report.

Due to the sharp rise in rates, new mortgage rates have continued to increase with high street lenders offering an average 75% LTV, two-year fixed rate product from 5.7%, and five-year fixed products from 5.2% (all rates are dependent on LTV and product fees). Although there has been another hike from the BoE, we expect these rates to stabilise. On a more positive note, four leading high street banks reduced their fixed rate last week for the first time since October 2022.

The UK labour market continues to be very tight, with the unemployment rate rising slightly to 4% in the three months to May. The number of people in employment remains high and the data shows an increase in the number of part-time employees over the last quarter. Labour demand has continued to ease with the number of vacancies falling over the quarter for the 12th consecutive period. Growth in regular pay, not including bonuses, was up by 7.3% in the three months to May. Although this is a 0.8% decline once adjusted for inflation, it represents another month of the largest growth rate seen outside of the coronavirus pandemic.

	Forecast in rates					
Effective Rate	**1mth time**	**3mth time**	**6mth time**	**12mth time**	**2yrs time**	**3yrs time**
Bank of England Base Rate*	5.25%	5.55%	5.70%	5.40%	4.56%	4.21%
2yr Fixed Rate**	5.36%	5.29%	5.16%	4.88%	4.39%	4.09%
3yr Fixed Rate**	5.08%	5.02%	4.90%	4.66%	4.24%	3.99%
5yr Fixed Rate**	4.68%	4.63%	4.53%	4.34%	4.05%	3.88%
10yr Fixed Rate**	4.22%	4.20%	4.16%	4.07%	3.94%	3.87%

* Using OIS Curve   **Based on the swap curve

The two-year swap rate is expected to slowly decline over the next three years, with three- and five-year swap rates predicted to follow the same pattern. All are falling at a far slower pace than previously thought. The curve has flattened slightly with the ten-year swap rate anticipated to stay relatively flat over the next year, decreasing by 35bps over the next three years.

UK Securitisation Market

The UK securitisation market has quietened down for the summer break, with Paratus (Foundation Home Loans), Together, and Lloyds taking advantage of the final window in mid-July. We are expecting a busy pipeline in September with c.10-12 UK RMBS transactions expected in the market. The key concerns of market participants continue to be the potential for deterioration of credit performance and higher than anticipated prepayments. It is still unclear whether issuers will be able to broadly syndicate their deals or work privately with investors.

This year so far, there has been just over £10 billion of UK RMBS paper placed into the market compared to approximately £20 billion at this time last year, although c.£12 billion of that was legacy paper. Due to wider market spreads and lower origination volumes, we have seen more prime issuances than specialist so far this year and only 40% of the specialist volumes we saw at this time last year.

This article was originally published on https://www.mortgagesolutions.co.uk on 09/08/2023

K M ART 0051 AUG23