

Economic Background and Borrowing Update

Economic Background

The fourth quarter of 2024/25 saw:

- GDP growth contracting by 0.1% m/m in January following a 0.4% rise in December, but worse than market expectations of a 0.1% gain;
- The 3myy rate of average earnings growth increased 5.8% in January, marking a slowdown from an upwardly revised 6.1% growth in the previous period;
- CPI inflation increase to 2.6% in November;
- Core CPI inflation increase from 0.4% m/m in February. The headline annual rate fell to 2.8% in February;
- The Bank of England kept Bank Rate unchanged at 4.5% during its March meeting, matching market expectations.

The UK economy contracted 0.1% m/m in January, following a 0.4% rise in December. The largest downward contribution came from the production sector which fell 0.9%, after a 0.5% rise in the previous period. Conversely, services expanded 0.1%, after a 0.4% rise in the previous period, led by administrative and support services and wholesale and retail trade. Elsewhere, the UK's trade deficit declined to £2.64 billion in January, down from £2.82 billion in December, marking the smallest trade gap since September.

The UK recorded a 144k rise in employment in the three months to January, following an upwardly revised 88k increase in the previous period, and significantly above market forecasts of a 95k rise. This marked the fastest job growth in three months. Meanwhile, average weekly earnings (including bonuses) increased 5.8% y/y in the three months to January, marking a slowdown from an upwardly revised 6.1% growth in the previous period.

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The Chancellor's Spring Statement saw fiscal policy tightened by around £9.7bn in 2029-30, reversing around 30% of the 1% loosening that was put in place last Autumn. Moreover, the Office for Budget Responsibility cut its forecasts for 2025 growth by half to 1% while pushing up their expectations for future years.

The Consumer Price Index increased 0.4% m/m in February, rebounding from a 0.1% drop in January and below forecasts of a 0.5% rise. The headline annual rate fell to 2.8% in February, down from 3% in the previous month, matching the Bank of England's forecasts. The largest downward contribution came from prices of clothing which declined for the first time since October 2021. In contrast, prices rose faster for transport, restaurants and hotels.

In the retail sector, overall sales increased 1% m/m in February, defying expectations of a 0.3% fall, following a downwardly revised 1.4% gain in the previous month. Sales in household goods stores surged, marking the strongest monthly gain since April 2021, with hardware stores having the largest upward contribution. Meanwhile, the GfK Consumer Confidence Index edged up to -19 in March, marking its second consecutive monthly increase, compared to -20 in February. Elsewhere, public sector net borrowing, excluding public sector banks, rose slightly to £10.7 billion in February from £10.6 billion a year prior, exceeding the expected £6.6 billion. Total public sector spending increased by £3.8 billion year-on-year, driven by higher departmental spending on goods, services, and local government operations.

UK inflation has proved somewhat stubborn throughout 2024/25. Having started the financial year at 2.3% y/y (April), the CPI measure of inflation briefly dipped to 1.7% y/y in September before picking up pace again in the latter months. The latest data shows CPI rising by 2.8% y/y (February), but there is a strong likelihood that figure will increase to at least 3.5% by the Autumn of 2025.

Against that backdrop, and the continued lack of progress in ending the Russian invasion of Ukraine, as well as the potentially negative implications for global growth as a consequence of the implementation of US tariff policies by US President Trump in April 2025, Bank Rate reductions have been limited.

Moreover, borrowing has becoming increasingly expensive in 2024/25. Gilt yields rose significantly in the wake of the Chancellor's Autumn Statement, and the loosening of fiscal policy, and have remained elevated ever since, as dampened growth expectations and the minimal budget contingency (<£10bn) have stoked market fears that increased levels of borrowing will need to be funded during 2025.

A summary overview of the future path of Bank Rate

The Bank of England sprung no surprises in their March meeting, leaving Bank Rate unchanged at 4.5% by a vote of 8-1, but suggesting further reductions would be gradual. The Bank of England was always going to continue its cut-hold-cut-hold pattern by leaving interest rates at 4.50% but, in the opposite of what happened at the February meeting, the vote was more hawkish than expected. This suggested that as inflation rises later in the year, the Bank cuts rates even slower, but the initial impact of President Trump's tariff policies in April 2025 on the financial markets underpin our view that the Bank will eventually reduce rates to 3.50%.

Borrowing

It is a statutory duty for the Council to determine and keep under review the "Affordable Borrowing Limits". The Council's approved Treasury and Prudential Indicators (affordability limits) are included in the approved Treasury Management Strategy. A list of the approved limits is shown in Appendix B. The Prudential Indicators were not breached during the second quarter of 2024/25 and have not been previously breached. The schedule at Appendix C details the Prudential Borrowing approved and utilised to date.

The Council had not undertaken any new borrowing for a number of years prior to taking out some short term borrowing in March 2024. The Council instead has been utilising cash balances to internally “borrow” for prudential borrowing schemes. This has enabled the Council to benefit from saving on interest costs compared to the returns that could be generated on the cash balances. This approach has been effective during a period where the Council has held significant cash balances.

Cash balances have now reduced as a result of reduced levels of reserves being held and loans continuing to reach their maturity dates. It has therefore been necessary to acquire new external borrowing during the fourth quarter of 2024/25, with new loans of £121.1m secured over short time periods (between 1 year and 2.5years). As these loans mature, the Council will be looking to take advantage of lower interest rates which are anticipated to reduce over this time period.

PWLB rates have reduced over the course of the financial year, which aligns with the reductions that have occurred with the Bank rate during the year. The table below shows the high/low/average PWLB rates for the 2024/25 financial year.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.77%	4.31%	4.52%	5.08%	4.88%
Date	26/02/2025	17/09/2024	17/09/2024	17/09/2024	17/09/2024
High	5.61%	5.34%	5.71%	6.18%	5.88%
Date	29/05/2024	13/01/2025	13/01/2025	13/01/2025	09/01/2025
Average	5.14%	4.86%	5.07%	5.56%	5.32%
Spread	0.84%	1.03%	1.19%	1.10%	1.00%