

Economic Background and Borrowing Update

Economic Background

The fourth quarter of 2025/26 saw:

- A 0.6% increase in real GDP in quarter 4 of 2025/26 compared to the previous 3 month period.
- Average wages excluding bonuses were 3.6% higher in the three months to February 2026 compared with the year before, and 0.4% higher after adjusting for inflation.
- CPI inflation increased to 3.3% in March 2026, up from 3.0% in February.
- The Bank of England's Monetary Policy Committee (MPC) left interest rates unchanged at 3.75% during the quarter.
- Gilt yields have risen materially in March 2026, more than reversing the falls earlier in the financial year.

UK real gross domestic product (GDP) is estimated to have increased by 0.6% in Quarter 1 (Jan to Mar) 2026, following revised growth of 0.2% in Quarter 4 (Oct to Dec) 2025. In output terms, all three sectors contributed to growth in the latest quarter; the largest contribution came from the services sector, growing by 0.8%.

Government borrowing in the 2025/26 financial year was £132 billion, which is £20 billion less than the amount borrowed in 2024/25. At the end of March 2026, public sector net debt was equivalent to 93.8% of GDP, compared to 93.2% a year before.

The loosening in the labour market continues to bear down on wage growth. The 3my growth rate of average earnings including bonuses slowed from 4.2% in December to 3.9% in January. Meanwhile, excluding bonuses, private earnings growth continued to fall from 3.4% to 3.3%.

UK consumer price inflation (CPI) in the fourth quarter of 2025/26 showed a trend of initial easing followed by a sharp uptick in March, primarily driven by external energy price shocks. After holding steady at 3.0% in January and February, the annual inflation rate rose to 3.3% in March 2026, largely due to rising motor fuel prices and travel costs following the escalation of conflict in the Middle East. The March rise, fuelled by a sharp increase in oil prices, exceeded earlier expectations of a decline to 2%. The Bank of England has noted risks that could drive inflation higher, with some forecasts suggesting it could move between 3% and 3.5% in the first and second quarters of 2026/27.

10-year Gilt yields have been exceptionally volatile in the final weeks of 2025/26, troughing at around 4.23% in late February before shooting up to 5.00% (and well through that on an intraday basis). That spike was driven by the outbreak of war in the Middle East, which prompted a dramatic reassessment of investors' Bank of England policy rate expectations. Having been pricing in rate cuts in late-February, as many as four rate hikes were discounted by late-March. The 10-year yield ended the quarter at

4.92% with around 65bp of rate hikes priced in over the coming year. In addition to more hawkish monetary policy expectations, part of this increase in yields probably reflected an increase in term premia amid concerns that the government may react by loosening the fiscal purse strings.

As for equity markets, the FTSE 100 experienced another volatile quarter, surging to an all-time high of around 10,900 in late February, leaving it up 10% from the start of 2026, before giving back most of those gains in March after the outbreak of the Middle East conflict. That pullback leaves the index at around 10,176 at the end of the quarter.

A summary overview of the future path of Bank Rate

There were two Monetary Policy Committee (MPC) meetings in the final quarter of the financial year. At the 4 February meeting, although disinflationary pressures remained, the committee noted that while inflation was above the 2% target, it was expected to fall back from April 2026. However, the economic impact of the escalating conflict was becoming a central concern and so the MPC voted 5-4 to hold rates at 3.75% rather than cut to 3.5%. The March meeting agreed unanimously to hold the bank rate at 3.75% acknowledging the conflict had caused swap rates to rise, leading to increased costs for fixed-rate mortgages. They emphasized a "gradual and careful" approach to any further withdrawal of monetary policy restraint, given that wage growth was slowing but services price inflation was still a factor.

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 fourth quarter of 2025/26 and have not been previously breached. The schedule at Appendix C details the Prudential Borrowing approved and utilised to date.

Cash balances have now reduced as a result of reduced levels of reserves being held and loans continuing to reach their maturity dates. Therefore, it has been necessary over the last 2 years to secure additional borrowing to reduce the under-borrowed position.

The Council has taken out £100m of new PWLB loans during the final quarter of 2025/26. This includes loans to replace loans that have matured, due to loans being taken over the last 2 years over a shorter maturity period whilst interest rates are higher. Also this encompasses £61.791m of borrowing relating to Exceptional Financial Support that was approved by the Government for 2025/26.

PWLB rates are based on gilt (UK Government bonds) yields through HM Treasury determining a specified margin to add to gilt yields. The main influences on gilt yields are Bank Rate, inflation expectations and movements in US treasury yields. Inflation targeting by the major central banks has been successful over the last 30 years in lowering inflation and the real equilibrium rate for central rates has fallen considerably due to the high level of borrowing by consumers: this means that

central banks do not need to raise rates as much now to have a major impact on consumer spending, inflation, etc. This has pulled down the overall level of interest rates and bond yields in financial markets over the last 30 years.

However, since early 2022, yields have risen dramatically in all the major developed economies, first as economies opened post-Covid; then because of the inflationary impact of the war in Ukraine in respect of the supply side of many goods. In particular, rising cost pressures emanating from shortages of energy and some food categories have been central to inflation rising rapidly. More recently, the Middle East conflict is likely to see inflation spike higher from late spring 2026 through to early 2027

Gilt yields have been volatile through 2025/26. The low point for long-term rates of 25 and 50 years' duration was reached early in April 2025 whilst the low points for short and medium dated rates were reached in early 2026, prior to the outbreak of the Middle East conflict.

At the close of 31 March 2026, the 1-year PWLB Certainty rate was 5.04% whilst the 5, 10, 25 and 50 year rates were 5.28%, 5.72%, 6.29% and 6.08% respectively.

The table below shows the high/low/average PWLB rates for the financial year.

	1 Year	5 Year	10 Year	25 Year	50 Year
Low	4.25%	4.56%	5.13%	5.78%	5.46%
Date	27/02/2026	27/02/2026	02/03/2026	04/04/2025	04/04/2025
High	5.28%	5.47%	5.88%	6.43%	6.24%
Date	23/03/2026	23/03/2026	27/03/2026	27/03/2026	27/03/2026
Average	4.52%	4.82%	5.38%	6.06%	5.81%
Spread	1.03%	0.91%	0.75%	0.65%	0.78%