



Arlingclose Ltd:
Independent treasury management services

Economic and Interest Rate Forecast

22nd December 2025

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- The Bank of England duly delivered on expectations for a December rate cut, but, despite softer economic data over the past two weeks, the minutes highlighted increased caution surrounding both the inflation outlook and the speed of future easing. With a close vote of 5-4 in favour of a rate reduction, this suggests that the bar for further monetary easing may be higher than previously thought despite the possibility of the CPI rate falling to target in 2026.
- Budget policies and base effects will mechanically reduce the CPI rate in 2026, on top of the downward pressure arising from soft economic growth and the looser labour market. However, many policymakers appear concerned that household and business inflation and pricing expectations are proving sticky following recent bouts of high price and wage growth, which may allow underlying inflationary pressure to remain elevated. While, the Bank's measure of household expectations ticked lower in December, it remains above levels consistent with the 2% target at 3.5%.
- While policymakers hold valid concerns, these appear somewhat out of line with current conditions; CPI inflation fell to 3.2% in November, private sector wage growth continued to ease amid the highest unemployment rate since the pandemic, and the economy contracted in October after barely growing in Q3. Business surveys pointed to marginally stronger activity and pricing intentions in December but also suggested that the pre-Budget malaise was not temporary. These data are the latest in a trend suggesting challenging economic conditions are feeding into price and wage setting.
- Risks to the growth and inflation outlook lie to the downside, which may ultimately deliver lower Bank Rate than our central case. However, the minutes suggest that the bar to further rate cuts beyond 3.25% is higher and the near-term upside risks to our Bank Rate forecast have increased. Having said that, we believe inflation expectations will naturally decline alongside headline inflation rates.
- Investors appear to have given the UK government some breathing space following the Budget, with long-term yields continuing to trade at slightly lower levels than in late summer/early autumn. Even so, sustained heavy borrowing across advanced economies, the DMO's move towards issuing more short-dated gilts and lingering doubts about the government's fiscal plans will keep short to medium yields above the levels implied by interest rate expectations alone.

	Current	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27	Mar-28	Jun-28	Sep-28	Dec-28
Official Bank Rate													
Upside risk	0.00	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central Case	3.75	3.50	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25
Downside risk	0.00	0.00	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
3-month money market rate													
Upside risk	0.00	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
Central Case	3.82	3.55	3.30	3.30	3.30	3.30	3.30	3.30	3.30	3.30	3.35	3.35	3.35
Downside risk	0.00	0.00	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
5yr gilt yield													
Upside risk	0.00	0.40	0.45	0.50	0.55	0.60	0.65	0.70	0.70	0.70	0.70	0.70	0.70
Central Case	3.96	3.85	3.80	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.80	3.80	3.80
Downside risk	0.00	-0.50	-0.60	-0.70	-0.80	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85
10yr gilt yield													
Upside risk	0.00	0.40	0.45	0.50	0.55	0.60	0.65	0.70	0.70	0.70	0.70	0.70	0.70
Central Case	4.52	4.40	4.35	4.30	4.30	4.30	4.30	4.30	4.30	4.30	4.35	4.35	4.35
Downside risk	0.00	-0.50	-0.60	-0.70	-0.80	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85
20yr gilt yield													
Upside risk	0.00	0.40	0.45	0.50	0.55	0.60	0.65	0.70	0.70	0.70	0.70	0.70	0.70
Central Case	5.16	5.00	4.95	4.90	4.90	4.90	4.90	4.90	4.90	4.90	4.95	4.95	4.95
Downside risk	0.00	-0.50	-0.60	-0.70	-0.80	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85
50yr gilt yield													
Upside risk	0.00	0.40	0.45	0.50	0.55	0.60	0.65	0.70	0.70	0.70	0.70	0.70	0.70
Central Case	4.74	4.65	4.60	4.60	4.60	4.60	4.60	4.60	4.60	4.60	4.65	4.65	4.65
Downside risk	0.00	-0.50	-0.60	-0.70	-0.80	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85	-0.85

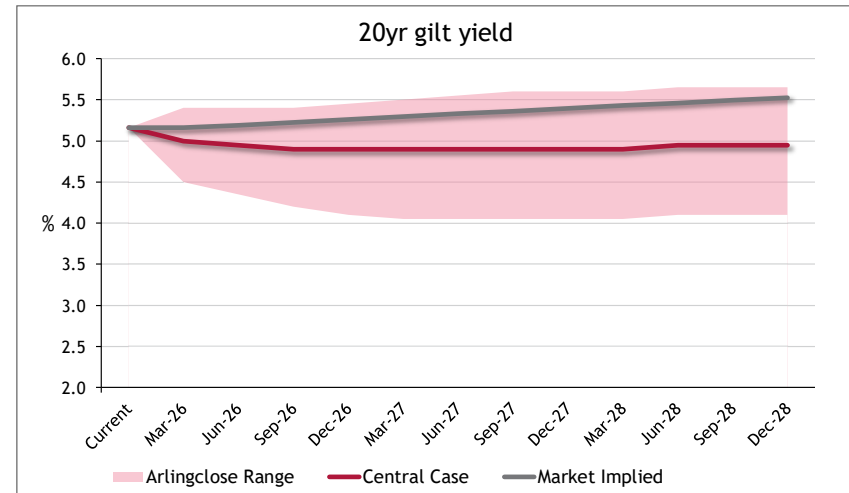
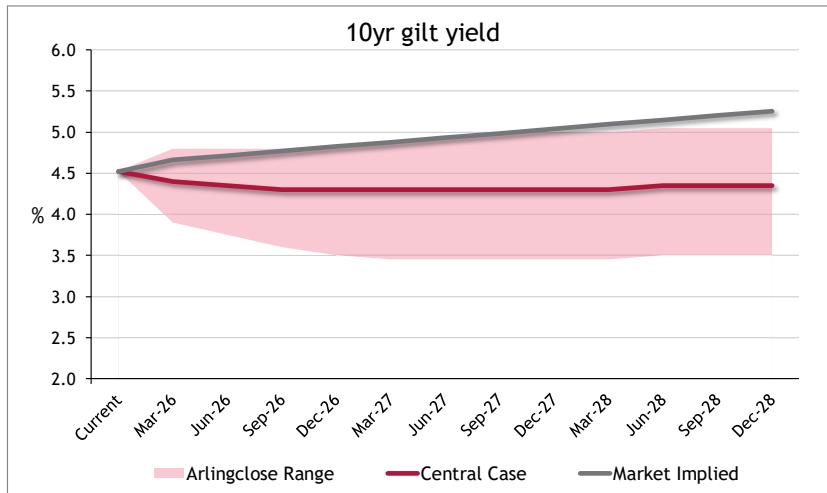
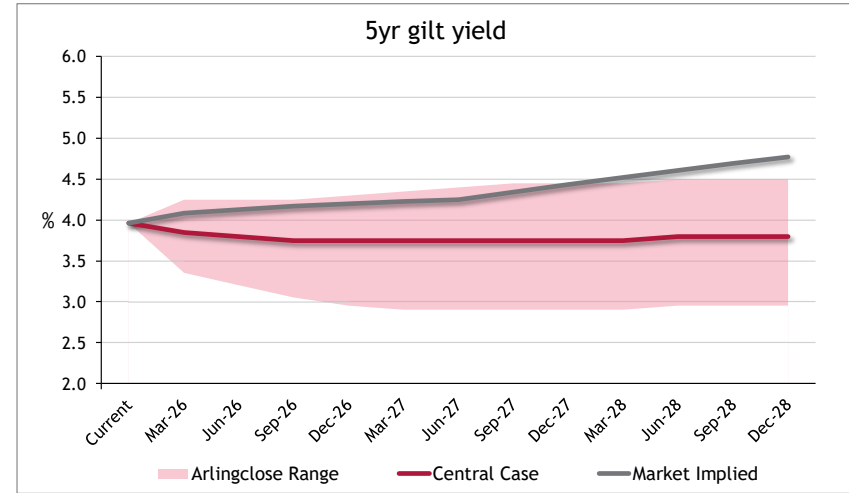
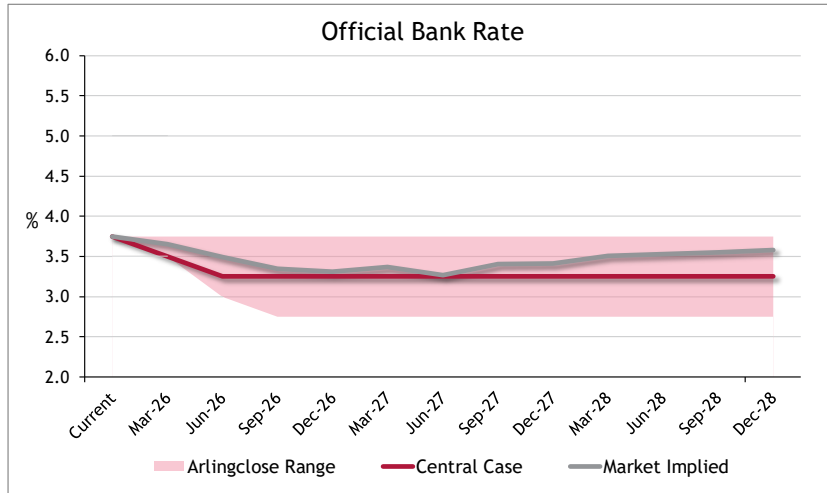
PWLB Standard Rate (Maturity Loans) = Gilt yield + 1.00%; PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%
 PWLB HRA Rate (Maturity Loans) = Gilt yield + 0.40%; National Wealth Fund Rate (Maturity Loans) = Gilt yield + 0.40%

- In line with our long-held forecast, Bank Rate was cut to 3.75% in December.
- Continuing disinflation, rising unemployment, softening wage growth and low confidence suggests that monetary policy will continue to be loosened.
- Arlingclose expects Bank Rate to be cut to 3.25% by middle of 2026. However, near-term upside risks to the forecast have increased.
- Medium and long-term gilt yields continue to incorporate premia for UK government credibility, global uncertainty and significant issuance. These issues may not be resolved quickly and we expect yields to remain higher than would normally be consistent with Bank Rate expectations.

Arlingclose and Market Projections

Charts show the Arlingclose central case along with upside and downside risks:

Arlingclose judges the risk around its Bank Rate and gilt yield forecasts to be weighted to the downside in the medium term.



Arlingclose forecast: 22nd December - versus - Market forward curves: 22nd December