INTEREST RATES

Recent history and its effect on interest rates in the UK

The Bank of England's key interest rate (Bank Rate) hit its most recent peak of 5.75% in July 2007. That was mere months before Northern Rock went bust, and we experienced a very visible bank run, with queues outside branches.

Northern Rock was the canary in the coal mine, as the US subprime mortgage crisis took hold, Lehman Brothers went bust and the panic began.

Since then, rates across the globe have plumbed record depths, and Bank Rate has been no different. To cushion against the financial crisis, the BoE dropped rates by 0.5% by March 2009. In August 2016, just after the UK voted for Brexit, rates went all the way down to 0.25%.

The world then witnessed what was a period of optimism on the return of growth, so in the years that followed; rates began to rise; up 0.5% in November 2017, then up again in August 2018.

Things looked wobblier in 2019 as China's economy slowed. The UK held rates steady as they probably didn't expect to see fresh record lows for interest rates in the near future.

And then the Coronavirus hit and in March 2020 the bank rate was slashed to 0.25%, and subsequently reduced even further to 0.1%, very close to an all time low.

That's where it's been ever since.

Now its almost certain that things are nearing a change, and we'll see rates rise.

Markets are beginning to price in a rate hike in December, and are already anticipating a further hike in Summer.

Financial markets predict and factor in a perceived change, and are now pricing in a hike in Bank Rate from 0.1% to 0.25% in December. They also see rates hitting 0.5% by August.

Why the rush to reprice? There are two main reasons. Firstly, inflation is rising and it's rising more rapidly than the Bank of England had expected. Secondly, the people who set interest rates (members of the Bank's Monetary Policy Committee) are now talking far more on the possibility of rate hikes. Elsewhere the BoE's governor, Andrew Bailey, told one news reporter that going forward they have a very delicate and challenging job on their hands. He warned that the Bank had to prevent high inflation expectations from becoming permanently embedded because that would obviously be very damaging.

I note that we are now seeing a shift, this can be seen by looking at Bailey's July statement – *'we shouldn't over-react to temporarily strong growth and inflation, to ensure that the recovery is not undermined by premature tightening in monetary conditions.'* The recent comments then are far from those made in July.

What does this mean for your money and loans?

Markets have become worried about the possibility of interest rate hikes, but it's worth remembering where we are, and what we are really looking at. The Bank of England rate is sitting at 0.1% right now, a record low, and we're talking about raising it to 0.5% in about six months. From a practical point of view is there a potential shock pending for the average real business, and or consumer, in terms of borrowing costs? The answer is, in my opinion, no.

The biggest debt cost for most consumers is their mortgage. Statistics show that about 80% of mortgage products sold in the UK are set at a fixed rate, and for the time being things may be ok, but those with a variable rate UK mortgage should now consider looking into a fixed rate. There are still some incredible deals to had out there.

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