

Our Savings Bulletin aims to provide you with the latest information on interest rates

Troubling economic data and continued worries about the global credit crunch were undoubtedly behind the Bank of England's decision to trim UK interest rates this month.

Commentators did not expect the nine-strong Monetary Policy Committee (MPC) to cut the cost of borrowing from 5.75% to 5.5%. Just days before the MPC's monthly meeting, the consensus among economists was that the rate-setters would hold off on any cuts until January or February due to continuing concerns about inflation.

Just hours ahead of the meeting, however, City economists at major banks and investment houses raced to revise their forecasts ahead of the first cut in interest rates since August 2005. Many are now predicting that rates could fall as low as 4.5% or even 4% by the end of 2008 after the committee, headed by governor Mervyn King, indicated it believes the economy is slowing down rather faster than it believes to be healthy.

The rate cut followed publication of figures that showed activity in the service sector, which makes up 70% of Britain's economy, has plunged to a four-year low. Commentators believe the overall economic outlook to be gloomy, pointing to a sharp decline in mortgage lending and faltering house prices, matched by a decline in commercial property prices.

Shoppers remain gloomier than they have been for three years with many retailers beginning their seasonal sales early. Economic indicators on the world stage are similarly down beat.

December's MPC meeting posed tough questions, according to some observers. The committee is wrestling with the issue of how best to tackle a slowing economy with rising inflation, while also dealing with consumers who have taken a knock in confidence, as well as embattled businesses and financial markets.

In a note accompanying the decision, the Bank of England said inflation remained its key concern. A slowing economy, the committee believes, will ease demand for oil and commodities, which alongside rate cuts would help keep inflation under the Bank's 2% threshold. Certainly the Bank has to strike a balance between inflationary pressures, while endeavouring to give a boost to business and consumer sentiment.

The rate cut is likely bring some relief to those householders on mortgages that track the Bank of England base rate, however. Some banks and building societies have already passed the cut on to borrowers. Whether they will be able to pass on further rate cuts in the New Year is debateable according to many commentators, due to the widening gulf between the Bank of England rate and the cost of funds in the wholesale money markets, a factor that has kept the cost of borrowing high for almost all lenders.

A further cut in interest rates is expected in the New Year.

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