Appendix A1

Commentary on the Economy and Interest Rates provided by Sector Treasury Services (April 2012)

Bank Base Rate

The original expectation for 2011-12 was that Bank Rate would start gently rising from quarter 4 2011. However, GDP growth in the UK was disappointing during the year under the weight of the UK austerity programme, a lack of rebalancing of the UK economy to exporting and weak growth in our biggest export market - the EU. The EU sovereign debt crisis grew in intensity during the year until February when a refinancing package was eventually agreed for Greece. This weak UK growth resulted in the Monetary Policy Committee increasing quantitative easing (QE) by £75bn in October and another £50bn in February. Bank Rate therefore ended the year unchanged at 0.5% while CPI inflation peaked in September at 5.2% but then fell to 3.4% in February, with further falls expected to below 2% over the next two years.

Gilt yields

Gilt yields fell for much of the year, until February, as concerns continued building over the EU debt crisis. This resulted in safe haven flows into UK gilts, which, together with the two UK packages of QE during the year, combined to depress PWLB rates to historically low levels.

Risk premiums

Risk premiums were also a constant factor in raising money market deposit rates for periods longer than 1 month. Widespread and multiple downgrades of the ratings of many banks and sovereigns, continued Euro zone concerns, and the significant funding issues still faced by many financial institutions, meant that investors remained cautious of longer-term commitment.