Interest rate rise could be lower than expected as markets rally

The financial markets have enjoyed a rebound as Boris Johnson dropped out of the leadership race, leaving Rishi Sunak as the favourite to become prime minister.

On Monday morning, the FTSE 100 started the day with a 0.5% rise, pushing it above the 7,000-point mark for the first time in a week.

And the pound rallied higher at $1.13. Those gains lessened as the day continued but was still up on Friday afternoon.

The value was higher than at most points over the last 10 days and follows the announcement that former prime minister **Mr Johnson** has exited the **Tory leadership race**.

There is also an expectation that a future rise in interest rates will be lower than previously forecast.

With the expectation that former chancellor **Mr Sunak** will become the next prime minister, the market reacted with the expectation he could fix the UK finances which have taken a hit over the past month when the pound reached an all-time low with the dollar and the Bank of England had to **intervene to prevent a collapse** in the pensions industry.

The rebound has come from a low on Friday afternoon where the pound was trading at $1.11, coinciding with the news Mr Johnson was seeking to once again be head of the Conservative Party.

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Friday morning had brought other bad financial news for the UK.

Moody’s rating agency was the latest to weigh in on the UK’s financial outlook. It was **cut down from “stable” to “negative”** due to policy uncertainty amid high inflation and weaker growth prospects.

Moody's said the government's "ability to engender confidence in its commitment to fiscal prudence" will be a consideration for Moody's in "resolving the negative outlook".

There were also concerns that the promised financial statement on 31 October, due to be delivered by Chancellor Jeremy Hunt, would be delayed by a new prime minister.

Similarly the pound fell against the euro shortly after midday on Friday to €1.13. This also rose on Monday morning to €1.15.

But today has been a positive morning for the UK finances across the board.

Markets are now expecting the **Bank of England** to set interest rates at slightly less than 5%, lower than the 6% expected in the weeks following the mini-budget.

That lower expected rate is likely to mean cheaper **mortgage repayments** for homeowners.

The cost of government borrowing also declined on Monday morning. The **interest rate** repayments the government has to pay on the money it borrowed on the market fell from 4.1% to 3.8% in its 10-year benchmark bonds, effectively state IOUs.

While some of those gains were lost as the morning moved to afternoon bonds were firmly back at pre-mini-budget levels.