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Private markets: Unknown unknowns

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Financial Services Regulation Committee

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See Appendix 1.

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Evidence is published online at <https://committees.parliament.uk/work/9235/growth-of-private-markets-in-the-uk-following-reforms-introduced-after-2008/publications/>.

Q in footnotes refers to a question in oral evidence.

SUMMARY

Global private markets have grown rapidly, from less than \$4 trillion in global assets under management in 2008 to around \$16 trillion today,¹ and approximately \$185 billion in the UK.² Whilst private markets have delivered strong returns for investors and provided tailored finance to UK companies and infrastructure projects, concerns have been raised about the implications of their rapid growth and interconnectedness with banks and insurers for the UK's financial stability. Our inquiry sought to shine a light on the drivers and consequences of the growth of private markets. Our key findings are as follows.

Global private markets, particularly private credit, are growing rapidly; the UK's position as a global financial centre means it will be the first to experience the opportunities and risks arising from this growth, particularly in US private markets.

Post-Global Financial Crisis regulatory reforms—particularly to bank capital requirements—have contributed to the growth of private credit, as banks have reduced direct lending to UK companies relative to non-banks and other types of lending.³ In addition, banks are increasingly relying on an 'originate to distribute' model of lending, in which private credit plays a significant role.

SME demand for borrowing has been subdued for some time. At the same time, the availability of SME finance has been squeezed by a combination of changes to bank capital and the fact that private credit has not entered the SME finance market. Addressing constraints on smaller and specialist banks' ability to lend could increase the finance available to SMEs, should demand increase.

There are insufficient data to conclude whether private markets are systemic, meaning there are considerable 'unknown unknowns'. The Bank of England is right to shine a light on the growth of private markets and their interconnectedness with the banking system through the voluntary System Wide Exploratory Scenario; the Committee supports the Bank in this endeavour, but it must move more swiftly and ensure its response to the outcome is proportionate to the risks identified. As collective memories may have faded, we must remain vigilant.

HM Treasury's evidence demonstrated a limited grasp of the concerns raised during this inquiry, which suggested passivity in the face of potential risks to the UK's financial stability arising from the growth of private markets. HM Treasury is responsible for ensuring overall financial stability so that the taxpayer does not serve as a backstop to the financial system.

1 Bank of England Financial Policy Committee, *Financial Stability Report July 2025*, July 2025, p 85

2 Written evidence from MSCI Ltd. (PMG0010)

3 Written evidence from the Bank of England (PMG0021); Written evidence from Positive Money (PMG0015)

Private markets: Unknown unknowns

CHAPTER 1: INTRODUCTION

Private markets

1. Private markets form an important part of the global financial system. The term ‘private markets’ generally refers to private equity funds and private credit funds, although the sector encompasses other forms of non-public investment such as venture capital, private real estate, and infrastructure finance.
2. Private markets are an important part of non-bank financial intermediation. The financial system is split broadly between bank intermediation and non-bank financial intermediation or ‘market-based finance’. Non-bank financial intermediation is a broad term that includes a range of financial activities, entities, and infrastructure outside the regulated banking system. Non-bank financial intermediaries comprise insurers, investment companies, hedge funds, and the asset managers which operate private equity and private credit funds. In outline:
 - (a) Private equity funds pool capital from institutional investors and high-net-worth individuals and invest this capital in target companies, typically with the objective of improving operational performance, restructuring, or facilitating growth. These funds realise returns through eventual sale or public listing.
 - (b) Private credit refers to debt financing provided to companies by non-bank lenders, typically private credit funds operated by asset managers. Unlike traditional corporate debt provided by banks or raised by bond issuance in public markets, private credit involves bilateral or club lending arrangements negotiated directly between borrowers and private lenders.
3. Globally, private markets have grown rapidly over the past 15 years and are playing an increasingly significant role in the financial system. The sector has grown from less than \$4 trillion in global assets under management in 2008 to around \$16 trillion today.⁴
4. Private markets are not subject to the same regulation as banks. Many funds and fund managers are based outside the UK, with the Financial Conduct Authority (FCA) serving as the primary regulator for those within the UK’s regulatory perimeter. The FCA supervises firms under the requirements set out by the Alternative Investment Fund Managers Regulations,⁵ which place requirements on governance, valuation, risk management and investor disclosures on the fund manager, rather than on the fund itself.⁶ Unlike banks, private market funds do not take deposits and are therefore not

4 Bank of England Financial Policy Committee, *Financial Stability Report July 2025*, July 2025, p 85

5 *The Alternative Investment Fund Managers Regulations 2013*. These Regulations continue to apply in the UK as assimilated law pursuant to the [European Union \(Withdrawal\) Act 2018](#) as amended by the [Retained EU Law \(Revocation and Reform\) Act 2023](#).

6 Written evidence from the Financial Conduct Authority ([PMG0040](#))

subject to the Prudential Regulation Authority’s (PRA) regime for regulating banks, which includes capital, liquidity, and resolution requirements, aimed at promoting the safety and soundness of firms.

5. Over recent years, private credit has become an increasingly important source of funding in the UK and worldwide. The European Leveraged Finance Association highlighted that:

“Prior to the Global Financial Crisis, larger businesses typically accessed public markets for funding, while mid-market and smaller companies relied primarily on bank lending. Today, banks continue to play a vital role in providing liquidity, operational facilities, and ancillary services. However, the majority of long-term lending to mid-market companies is now provided by private debt funds. The growth of private credit has enabled these funds to offer increasingly large-scale financings, including multi-billion-pound debt packages that were previously the domain of bond markets or broadly syndicated loans.”⁷

Concerns about private markets

6. Private markets have increasingly attracted attention from regulators, who have raised concerns about potential risks arising from the rapid growth of private markets and the banking sector’s growing exposure to them. The Bank of England stated that the growth of private markets “has been an area of increasing focus for the Bank of England, other UK regulators, international organisations and global bodies focused on financial stability.”⁸
7. The International Monetary Fund (IMF) has expressed repeated concerns about private markets, particularly private credit. Its April 2024 Global Financial Stability Report warned: “Credit migrating from regulated banks and relatively transparent markets—such as syndicated loans or corporate bond markets—to the opaque world of private credit creates potential risks. While immediate risks may seem contained, the sector has meaningful vulnerabilities.”⁹ Similarly, the Financial Policy Committee’s July 2025 Financial Stability Report identified three fundamental features of private markets that could cause systemic risks: “the widespread use of leverage, the opacity of valuations and extent of reliance on rating agencies, and the correlation with other risky funding markets.”¹⁰ Recently, the Financial Stability Board has also stated that assessing the impact of private assets will be “an important part of the FSB’s [Financial Stability Board’s] surveillance work in the year ahead.”¹¹
8. The collapse of two US companies—First Brands, a car parts supplier, and Tricolor, a sub-prime auto lender—has raised fears about weakening lending standards in the private credit market.¹² Regarding these companies, Andrew Bailey, the Governor of the Bank of England, said the question being asked

7 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

8 Written evidence from the Bank of England ([PMG0021](#))

9 International Monetary Fund, *Global Financial Stability Report, Chapter 2 Summary*, April 2024, p 1. See also: International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025

10 Written evidence from the Bank of England ([PMG0021](#)). See also: Bank of England Financial Policy Committee, *Financial Stability Report July 2025*, July 2025, pp 85–90

11 Financial Stability Board, *Letter to G20 Leaders*, 18 November 2025, p 2

12 Financial Times, *‘Top US financiers sound alarm on lending standards’*, 15 October 2025. Lending standards are the criteria and guidelines that a lender uses to evaluate a loan application.

was “are these cases idiosyncratic or are they what I call the canary in the coal mine?”¹³

Our inquiry

9. The growth of private markets in the UK has been accompanied by a shift in the patterns of lending to the real economy, with non-bank financial intermediaries accounting for a growing share of lending relative to banks. Although banks remain the dominant provider of lending in the UK economy, the proportion of total lending to the real economy they provide has declined from 85% in 2008 to 80% in 2024.¹⁴
10. The Committee’s previous report on the FCA and PRA’s secondary growth and competitiveness objective, *Growing Pains: Clarity and Culture change required*, published in July 2025, highlighted concerns about the impact of the reforms to the UK’s regulation of bank capital and liquidity requirements introduced following the Global Financial Crisis in 2008. These reforms to bank regulation sought to ensure that banks maintain levels of capital and liquidity that better reflect the risks of their assets, to ensure they can absorb losses and remain stable, providing more sustainable support to the real economy. Although these reforms provided improved levels of financial resilience, we concluded that one unintended consequence of the PRA’s approach to setting capital requirements has been that it has limited the commercial incentives and capital available to provide finance for growth. Hence, we recommended that the PRA should consider a more proportionate approach.¹⁵
11. This inquiry builds on these findings in view of the increasing interest in, and growing concerns about, the growth of private markets, particularly private credit. We sought to examine the extent to which bank regulatory capital and liquidity requirements since 2008 have contributed to this growth, the changes in the UK’s lending landscape, and the availability of credit for small and medium-sized enterprises (SMEs). Our inquiry also examined the concerns that regulators have expressed around the implications of the growth of private markets for financial stability.
12. Our inquiry was launched on 2 July 2025. Over the course of the inquiry, we received 48 pieces of written evidence and heard oral evidence from 29 witnesses.
13. We are grateful to all those who submitted evidence to the inquiry. All of those who provided evidence are listed in Appendix 2. A list of Members’ interests is contained in Appendix 1. We also want to thank our Specialist Advisers, Professor Rosa Lastra and Michael Raffan, for the support and guidance given throughout the inquiry.

13 [Q 107](#) (Andrew Bailey)

14 Written evidence from the Bank of England ([PMG0021](#))

15 Financial Services Regulation Committee, *Growing pains: clarity and culture change required An examination of the secondary international competitiveness and growth objective* (2nd report, Session 2024–25, HL Paper 133)

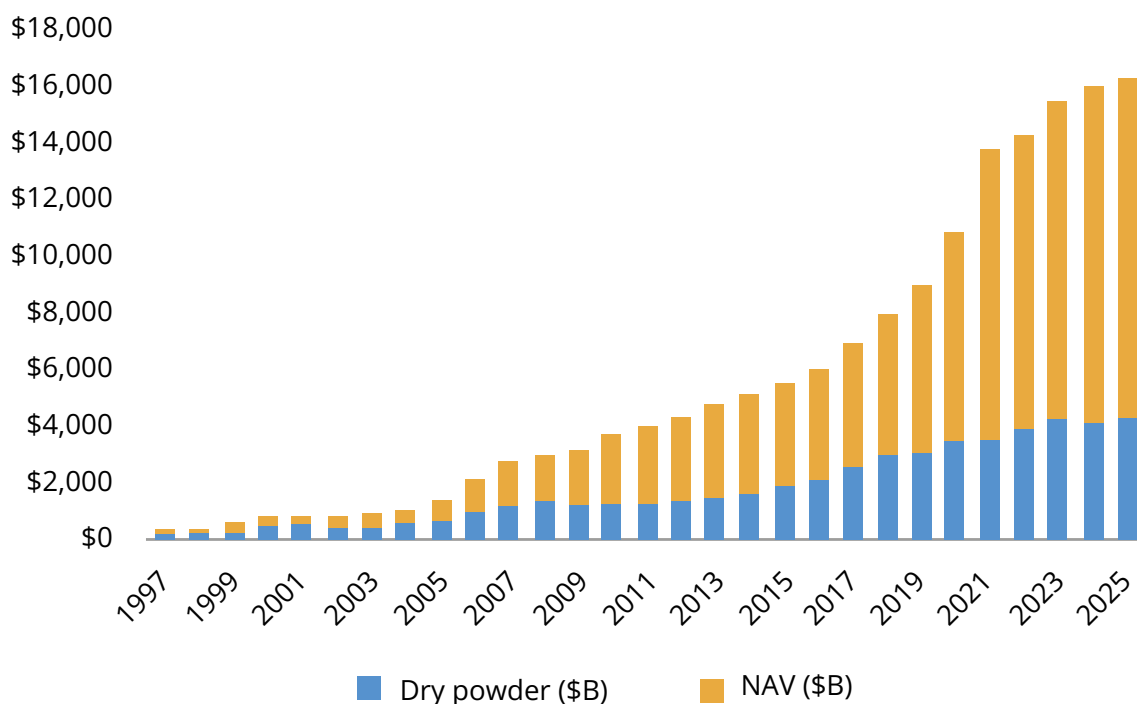
CHAPTER 2: GROWTH OF PRIVATE MARKETS

14. Examining why private markets, particularly private credit, have grown since the Global Financial Crisis underpinned our inquiry. Notably, we sought to understand the extent to which the increase in regulatory bank capital and liquidity regulatory requirements have contributed to their rapid growth. The key trends we identified include the growing importance of private credit, the relative retreat of banks from certain types of lending, and what this means for the broader lending ecosystem.

The growth of private markets since 2008

15. As noted in paragraph 3, private markets globally have grown substantially since 2008.¹⁶ This growth has been most significant in the US, which accounts for approximately three-quarters of private markets' global value,¹⁷ followed by the UK as the second largest private market.¹⁸ UK private markets have experienced significant growth, with total capitalisation reaching approximately \$185 billion in the first quarter of 2025, an increase of 56% from 2015.¹⁹ Witnesses emphasised that private markets, particularly private credit, are increasingly important to UK businesses and will continue to grow rapidly.²⁰

Figure 1: Global private market assets under management [\$USD billion]



Source: Written evidence from the Bank of England ([PMG0043](#)) and PitchBook

16. The Bank of England shared data on the growth of global private markets by assets under management. Figure 1, above, shows assets under management by private market finance, which includes: private credit, private equity,

16 Written evidence from the Association for Financial Markets in Europe ([PMG0017](#))

17 Written evidence from Professor Marco Lamandini and Professor David Ramos Muñoz ([PMG0007](#))

18 Written evidence from the British Venture Capital & Private Equity Association ([PMG0016](#))

19 Written evidence from MSCI Ltd. ([PMG0010](#))

20 Written evidence from the Association for Financial Markets in Europe ([PMG0017](#)); Written evidence from TheCityUK ([PMG0009](#))

venture capital, debt vehicles such as real estate funds, funds-of-funds and other niche assets. The data in Figure 1 include dry powder (capital committed to a fund by an investor that has not yet been deployed), and net asset value (total assets minus total liabilities).

Trends in private equity

17. The Bank of England noted that private equity is “the most prominent form of private markets activity”²¹, and has grown from \$2 trillion to \$8 trillion in global assets under management over the last decade.²² In line with global trends, private equity represents a considerable proportion of the UK’s private markets. The British Venture Capital & Private Equity Association told us that private equity and venture capital back approximately 13,000 UK companies, which employ 2.5 million people, and generate £199 billion in GDP; this represents 8% of total employment, 7% of UK GDP, and 9% of gross earnings.²³

Trends in private credit

18. The Bank of England estimates that global private credit assets under management have increased from approximately \$0.2 billion in the early 2000s to over \$2.5 trillion in 2025.²⁴ This is expected to rise to \$3 trillion by 2028.²⁵ This growth has been led by the US, followed by the UK and the EU. Private credit loan issuance is indicative of this, growing 500% in the US, 285% in the UK, and 130% in the EU between August 2022 and April 2024.²⁶ UK private markets, although growing more slowly than those in the US, have nevertheless experienced significant growth. Analysis by UK Finance indicates that there was no outstanding private credit debt in the UK in 2013, increasing to £59.5 billion in 2024, a compound annual growth rate of 43%.²⁷
19. We received evidence that trends in UK private markets, as the second largest globally,²⁸ closely mirror developments in the US. Dr Narine Lalafaryan, Assistant Professor of Corporate Law, University of Cambridge, told us that “US investment funds are introducing their trends all over the world, and the UK is a market these investors find it very easy to navigate due to our legal system because it is very flexible.”²⁹ Consequently, “London is the first global hub where these trends are being tested, redefined and amended—and, sometimes, rejected.”³⁰
20. **The rapid growth of global private credit and equity markets, particularly in the US, presents opportunities and risks for the UK. The Committee welcomes the Bank of England’s work to shine a light on these developments; the Government, the Bank of England, the Prudential Regulation Authority, and the Financial Conduct**

21 Written evidence from the Bank of England ([PMG0021](#))

22 *Ibid.*

23 Written evidence from the British Venture Capital & Private Equity Association ([PMG0016](#))

24 Written evidence from the Bank of England ([PMG0021](#))

25 Written evidence from The Association for Financial Markets in Europe ([PMG0017](#))

26 Written evidence from the Managed Funds Association ([PMG0012](#))

27 UK Finance, *UK Public and Private Capital Markets*, March 2025, pp 10, 14–15

28 Written evidence from the British Venture Capital & Private Equity Association ([PMG0016](#)); [Q 16](#) (Dr Narine Lalafaryan)

29 [Q 16](#) (Dr Narine Lalafaryan)

30 [Q 27](#) (Dr Narine Lalafaryan)

Authority must continue proactively to monitor developments in private markets.

Drivers of private market growth

21. The evidence we received associated the rapid growth of private markets with two primary factors. First, banks have changed the focus of their lending activity away from certain sectors, in part caused by regulation introduced following the Global Financial Crisis, into which private markets have expanded. Second, private markets, particularly private credit, have grown in response to increased demand from institutional investors for higher returns, and borrowers for flexible, diversified sources of finance. Additionally, private credit may be better suited to longer term lending, for example to infrastructure projects given the longer-term nature of investment in private credit funds, which has led to a greater involvement of pension funds and insurance companies in the provision of private credit.

Changes in bank lending

22. The evidence we received indicated that the amount and type of lending that banks provide has changed since the Global Financial Crisis and has created the conditions that have allowed private markets to grow; much of the evidence attributed this development to regulation introduced following the Global Financial Crisis.³¹ Whilst bank lending accounted for approximately 80% of the total stock of direct lending to the real economy (households and private non-financial corporations) in 2024, this represents a decrease from 85% in 2008.³² The Bank of England noted that this shift is “most pronounced in corporate lending.”³³ Specifically, Professor Simon Gleeson, Visiting Professor, Faculty of Law at the University of Oxford, noted: “Over the last two decades, non-banks have accounted for the entirety of the cumulative increase in new corporate lending in the UK, and non-bank financial institutions now account for 50% of the stock of corporate lending.”³⁴

The impact of post-2008 capital and liquidity requirements

23. Post-2008 reforms to bank regulation significantly increased the amount of capital the banks must hold against their assets, particularly those deemed to be higher risk. As the Bank of England highlighted, before 2008 “banks had taken unsustainable risks and had insufficient capital and liquidity resources to absorb adverse shocks given the risks they had taken.”³⁵ Much of the evidence indicated that the post-2008 reforms have significantly improved financial stability and have been successful in de-risking traditional lenders.³⁶ Lord King of Lothbury, former Governor of the Bank of England, emphasised that these reforms were, in part, designed to create such a shift: “One of the responses to the financial crisis was to suggest that the banking system ought to do fewer of the activities in which it had been engaged, in order to make it safe for depositors, and that the risky activities should go to something outside the banking sector.”³⁷

31 [Q 67](#) (Lord King of Lothbury); Written evidence from Professor Raghavendra Rau ([PMG0036](#)); [Q 82](#) (Nigel Terrington); Written evidence from Sheila Bair ([PMG0026](#))

32 Written evidence from the Bank of England ([PMG0021](#))

33 *Ibid.*

34 [Q 1](#) (Professor Simon Gleeson)

35 Written evidence from the Bank of England ([PMG0021](#))

36 *Ibid.*; Written evidence from Professor Raghavendra Rau ([PMG0036](#)); Written evidence from Professor Eilís Ferran FBA ([PMG0024](#))

37 [Q 67](#) (Lord King of Lothbury)

24. The evidence was consistent in suggesting that the post-2008 reforms have caused banks to retreat from some sectors and resulted in some lending migrating from the banking sector into private markets. Professor Raghavendra Rau, Sir Evelyn de Rothschild Professor of Finance at the University of Cambridge, stated that the reforms have had “a direct impact on banks’ ability and willingness to engage in certain types of lending.”³⁸ He went on to elaborate: “With balance sheet lending becoming significantly more costly, banks were incentivised to retrench from segments of the market that offered lower returns relative to the new capital requirements.”³⁹ Similarly, the European Leveraged Finance Association told us: “These reforms have reshaped the risk-return dynamics for banks, leading to a retreat from certain lending segments.”⁴⁰
25. Nigel Terrington, Chief Executive Officer of Paragon Bank, told us that: “There is probably 300% to 400% increase in capital today, relative to where it was pre-financial crisis”.⁴¹ Charlie Nunn, Chief Executive Officer of Lloyds Banking Group, also drew attention to the cost of capital, telling us that systemically important UK banks are subject to regulatory capital requirements of approximately 12%.⁴² Nigel Terrington noted that this increase in bank capital requirements has caused “some level of lending or activity to be almost disregarded—kind of rejected—from the banking sector. That has allowed the growth and proliferation of the private credit markets.”⁴³
26. We received evidence that banks have reduced the volumes they lend directly to higher-risk market segments relative to lower-risk lending. Positive Money indicated that “the ratio of lending to the real economy relative to mortgage lending fell drastically from 0.28 to 0.17.”⁴⁴ Specifically, the proportion of bank lending allocated to mortgages increased from 39.7% in December 2008 to 54% in June 2025, with lending to non-financial companies falling from 11.6% in July 2009 to 9.6% in June 2025.⁴⁵ Positive Money explained that: “Under [the Basel framework’s] capital adequacy ratios, lending against property typically offers the best return on equity for banks”.⁴⁶ Equally, they noted: “Liquidity requirements, such as the liquidity coverage ratio, reduce banks’ ability or willingness to use deposit funding to provide finance to the real economy”.⁴⁷
27. Furthermore, we received evidence that lower risk weights⁴⁸ on lending to private market firms make it more capital efficient for banks to lend into private markets rather than directly to companies. Michael Roberts,

38 Written evidence from Professor Raghavendra Rau ([PMG0036](#))

39 Written evidence from Professor Raghavendra Rau ([PMG0036](#))

40 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

41 [Q 85](#) (Nigel Terrington)

42 [Q 147](#) (Charlie Nunn)

43 [Q 82](#) (Nigel Terrington)

44 Written evidence from Positive Money ([PMG0015](#))

45 *Ibid.*: Non-financial companies are “businesses operating in the real economy (excluding finance, insurance, and the real estate industries)”.

46 Written evidence from Positive Money ([PMG0015](#))

47 *Ibid.*

48 The risk weighting of assets measures the relative risk of a given asset defaulting (credit risk), thus incurring financial loss. The risk weighting is applied to the value of an asset to provide risk-weighted assets (RWAs), which is then used to calculate the amount of capital that a bank must hold. The PRA has the power to set risk weightings under the Capital Requirement Regime, which it generally sets in line with international standards, set out in the Basel Framework promulgated by the Basel Committee on Banking Supervision.

Chief Executive Officer of HSBC Bank plc and Chief Executive Officer of Corporate and Institutional Banking at HSBC, noted that lending to private credit firms on a securitised basis “gets certain preferable treatment under the Basel regimes, so that becomes a less capital consumptive form of lending.”⁴⁹ Specifically, “if we lend to exactly the same borrowers but we do not do so on a securitised basis—so we lend directly to them—the capital requirement is 100% against the loan itself [...] and 20% against the securitisation.”⁵⁰ Professor Kern Alexander Chair for International Financial Law and Regulation, University of Zurich, and Director of Studies in Law and Finance, Queens’ College at the University of Cambridge, provided the example of Apollo Global Management’s \$6 billion loan to InBev, telling us that “JP Morgan made the \$6 billion loan [...] to Apollo Global Management for that deal. The risk weighting on that loan by JP Morgan is lower than if JP Morgan had made that loan directly”⁵¹.

28. On 2 December 2025, the Financial Policy Committee published the outcome of its review ‘Financial Stability in Focus: The Financial Policy Committee’s assessment of bank capital requirements’, in which it has reduced the benchmark for Tier 1 capital⁵² which banks across the sector are required to hold from 14% to 13% of risk weighted assets.⁵³ Further work will be carried out on other aspects of the regulatory capital framework.

Capital buffers

29. The PRA and the Bank of England have the discretion to set the rate of the capital buffers applied to the banking system.⁵⁴ Capital buffers are additional capital requirements which regulators require banks to hold in excess of their minimum requirements, with the intention for these to be drawn down during times of stress to ensure that banks can continue to lend into the economy.
30. However, Michael Roberts indicated that these buffers are treated as permanent additions to banks’ balance sheets: “Buffers—both liquidity and capital buffers—are there to not to be used. [...] There certainly is a very detrimental perception that, if you use your buffers, you are being far too aggressive in how you are running the bank.”⁵⁵ Professor Kern Alexander explained that, were a bank to use its buffers, they would “need to be rebuilt later under supervisory control and timetable. And the market knows this. As a result, whether these buffers can really be used [...] without the risk of creating a loss of confidence by the market is debatable.”⁵⁶ The Financial Policy Committee has announced that it will be reviewing the usability of capital buffers.⁵⁷

49 [Q 165](#) (Michael Roberts)

50 *Ibid.* See also: Written evidence from Sheila Bair ([PMG0026](#))

51 [Q 6](#) (Professor Kern Alexander)

52 Bank of International Settlements, *Definition of capital in Basel III—Executive Summary*, June 2019, p 1: “Common Equity Tier 1 capital (CET1) is the highest quality of regulatory capital, as it absorbs losses immediately when they occur.”

53 Bank of England Financial Policy Committee, *Financial Stability in Focus: The FPC’s assessment of bank capital requirements*, December 2025, p 45

54 Prudential Regulation Authority, *PRA Rulebook, Capital Buffers*. See also: Financial Services and Markets Act 2000, [Part 9D](#).

55 [Q 170](#) (Michael Roberts)

56 Written evidence from Professor Kern Alexander ([PMG0028](#))

57 Bank of England Financial Policy Committee, *Financial Stability in Focus: The FPC’s assessment of bank capital requirements*, December 2025, p 59

31. David Postings, Chief Executive Officer of UK Finance, highlighted the countercyclical capital buffer, which the UK sets at 2%, whereas the EU and US set this at 1% and 0% respectively.⁵⁸ The evidence relating to capital buffers mirrors the findings and conclusions from our previous report, that a culture of risk aversion has developed within the regulators, driven by the repercussions of the Global Financial Crisis and the conflicting pressures under which the regulators operate.⁵⁹

Impact of broader regulatory requirements

32. Alongside the impact of capital and liquidity requirements, several witnesses suggested that reforms to conduct regulation have also increased banks' risk aversion and made it harder to engage with businesses. The Investment Association told us that some regulations, including conduct rules, "sometimes make [banks] less nimble or willing. Private markets are less constrained by conduct rules [...] allowing them to negotiate more freely with sophisticated counterparties."⁶⁰ Similarly, the European Leveraged Finance Association told us that: "Regulatory requirements have also increased the complexity of operational and compliance processes, such as ring-fencing, which can make engagement with banks more challenging for some businesses."⁶¹
33. David Postings told us that "the conduct environment [...] has created a certain degree of risk aversion inside the organisations",⁶² and suggested that the Senior Manager and Certification Regime (SM&CR) is indicative of this: "When you are individually subject to something such as that, it makes you cautious. [...] It makes you think very carefully about whether the outcome is going to be a good one, and so people become less willing to take risk in all forms."⁶³
34. **Reforms introduced after the Global Financial Crisis—particularly bank capital and liquidity regulatory requirements—have, as intended, encouraged the banking system to retreat from riskier lending, leaving certain segments of the economy, including SMEs, less well served by banks.**

Market conditions and demand from investors and borrowers

35. Whilst the evidence indicated that reforms to banking regulation have contributed to the growth of private markets, it was also clear that market conditions following the Global Financial Crisis have supported the expansion of private markets. First, the period of prolonged low interest rates and large-scale quantitative easing⁶⁴ following 2008 increased the amount of capital flowing into the sector. Additionally, private credit firms have

58 [Q 101](#) (David Postings)

59 Financial Services Regulation Committee, *Growing Pains: Clarity and Culture Change Required. An examination of the secondary international competitiveness and growth objective* (2nd report, Session 2024–25, HL Paper 133) p 27

60 Written evidence from the Investment Association ([PMG0013](#))

61 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

62 [Q 100](#) (David Postings)

63 [Q 100](#) (David Postings)

64 Economic Affairs Committee, *Quantitative easing: a dangerous addiction?* (1st Report, Session 2021–22, HL Paper 42) p 8: "Quantitative easing is a monetary policy tool that central banks can use to inject money into the economy through the purchase of 'financial assets', usually government bonds. Quantitative easing is also known as 'asset purchasing'."

benefitted from higher demand from corporate borrowers for the flexible financing they provide.⁶⁵

Low-interest rate environment and quantitative easing

36. Quantitative easing and the low-interest environment following the Global Financial Crisis were repeatedly identified as key drivers behind the growth of private markets.⁶⁶ The period of low interest rates reduced the attractiveness of traditional asset classes, as the Bank of England stated, the “prolonged period of low yields prompted investors to seek higher returns.”⁶⁷ Ignazio Angeloni, Fellow at the Institute for European Policymaking, Bocconi University, and Senior Policy Fellow at SAFE, Goethe University, explained that low-interest rates “rendered bank intermediation less profitable and led investors to search for more attractive returns outside the banking sector.”⁶⁸
37. Similarly, TheCityUK suggested that quantitative easing has “increased the supply of money in the financial system and encouraged the search for yield outside traditional banking channels.”⁶⁹ Professor Ludovic Phalippou, Professor of Financial Economics at the Saïd Business School, University of Oxford, told us that quantitative easing had a notable impact on the attractiveness of traditional long-dated assets, as investments would provide “zero or even negative interest rates if you left it in bonds”.⁷⁰
38. Dr Daniele D’Alvia, Lecturer in Banking and Finance Law and Associate Researcher at the European Banking Institute at Queen Mary University of London, told us that this dynamic “drove investors to seek higher yields in private markets”.⁷¹ Professor Raghavendra Rau suggested that: “With returns on traditional fixed-income assets suppressed, these investors were compelled to look further afield to meet their long-term liabilities. Private credit, offering higher contractual returns and an illiquidity premium, emerged as a highly attractive asset class.”⁷² Specifically, the Bank of England noted that private markets “offered investors higher prospective returns, lower measured volatility, and therefore higher apparent risk-adjusted returns than in public markets.”⁷³

Market-driven growth of private credit

39. The evidence indicated that the particularly rapid growth of private credit is attributable to market demand for the finance that these funds can provide. Witnesses suggested that the business model and funding structure of private credit makes it well placed to meet the needs of UK corporate borrowers.
40. First, private credit is an attractive provider of patient capital. Daniel Leiter, Senior Managing Director and Head of International & Global Head of Liquid Credit Strategies at Blackstone, explained that private credit funds “are long-term investors that originate to hold to maturity.”⁷⁴ This provides

65 Written evidence from the Bank of England ([PMG0021](#))

66 Written evidence from Ignazio Angeloni ([PMG0023](#)); Written evidence from TheCityUK ([PMG0009](#)); Written evidence from Dr Daniele D’Alvia ([PMG0008](#)); [Q 26](#) (Professor Ludovic Phalippou)

67 Written evidence from the Bank of England ([PMG0021](#))

68 Written evidence from Ignazio Angeloni ([PMG0023](#))

69 Written evidence from TheCityUK ([PMG0009](#))

70 [Q 26](#) (Professor Ludovic Phalippou)

71 Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

72 Written evidence from Professor Raghavendra Rau ([PMG0036](#))

73 Written evidence from the Bank of England ([PMG0021](#))

74 [Q 135](#) (Daniel Leiter)

certainty for borrowers, as Professor Ludovic Phalippou noted: “You will not have to deal with anyone else [...] That is massively attractive for a borrower.”⁷⁵ Private credit matches this longer-tenure debt with funding from “committed, long-term capital, such as from pension funds, insurers, other institutional investors [...] in other words our funding matches the life of our loans.”⁷⁶

41. Second, as private credit typically holds loans to maturity, they are well placed to develop relationships with borrowers, as Blair Jacobson, Partner and Co-President at Ares Management Corporation, noted: “We have multi-year relationships, can invest more capital, and get a good return, and they can use that capital to grow”.⁷⁷ These relationships allow private credit to provide “more than just finance, with board-level and strategic support, sector experience, networks, and potential for follow-on capital.”⁷⁸ Daniel Leiter noted that Blackstone has “programmes to help these companies grow [...] we help them find operational synergies and with procurement and even cybersecurity, et cetera.”⁷⁹
42. Third, witnesses indicated that such bi-lateral relationships benefit from private credit’s use of unitranche loans, “where one private lender provides a big chunk that would have been a mix of senior and junior bank debt.”⁸⁰ The Investment Association characterised this as a “one-stop-shop capacity”⁸¹ which can be attractive to borrowers as these involve only one set of documents and one counterparty.⁸² Professor Ludovic Phalippou outlined how, unlike a syndicated bank loan, private credit is able to provide “£60 million today, no questions asked”.⁸³
43. Fourth, the evidence we received underscored the speed and flexibility of private credit loans. Dr Narine Lalafaryan, told us that private financing “is much faster to obtain it—it is speedier. It is more costly than bank financing, but there is more flexibility for companies.”⁸⁴ Moreover, the Investment Association noted that funds can “structure a loan in creative ways (e.g., second-lien, PIK [payment in kind] interest, bullet repayment, equity kickers) to suit a company’s needs”.⁸⁵ Such flexibility is particularly attractive to corporations which “accumulated significant debt during the low-rate environment of the past decade, and in the current higher-rate context face rising costs and re-financing challenges.”⁸⁶
44. **The rapid growth of private credit and private equity is a response to market demand for assets that provide higher returns from institutional investors during a period of relative lower yields, and greater flexibility for borrowers. Quantitative easing and low interest rates have helped to create these market conditions.**

75 [Q 19](#) (Professor Ludovic Phalippou)

76 [Q 131](#) (Daniel Leiter)

77 [Q 140](#) (Blair Jacobson)

78 Written evidence from the British Venture Capital & Private Equity Association ([PMG0016](#))

79 [Q 134](#) (Daniel Leiter)

80 Written evidence from the Investment Association ([PMG0013](#))

81 *Ibid.*

82 *Ibid.*

83 [Q 19](#) (Professor Ludovic Phalippou)

84 [Q 19](#) (Dr Narine Lalafaryan)

85 Written evidence from the Investment Association ([PMG0013](#))

86 Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

45. **Private credit currently remains a small provider of corporate debt in the UK, relative to banks. However, the rapid growth of private credit is likely to continue, and we expect it to become an increasingly significant provider of corporate direct lending.**

Implications for the UK lending landscape

46. Witnesses suggested that due to regulatory change and market developments following 2008, the business lending landscape has significantly diversified. Dr Daniele D’Alvia highlighted that the corporate debt landscape has increasingly shifted to a “dual-track’ or even ‘triple-track’ process where companies can choose between bank loans, private credit, and capital markets, or combine them.”⁸⁷
47. The data on the total volume of lending provided by private credit, in particular corporate debt, in the UK are limited.⁸⁸ Noting the gaps in available data, the Bank of England’s analysis suggested that private credit deals involving UK headquartered companies total close to £400 billion since 2005.⁸⁹ Currently, non-financial companies have private debt arrangements worth £100 billion, £80 billion of which has been drawn; this represents 5% of total UK corporate debt, and 2% of overall lending to the UK economy.⁹⁰
48. Additionally, it is important to note that we received evidence from private credit firms which lend directly, primarily to investment grade companies, presenting only a partial picture of the market. For instance, we did not receive evidence from private credit firms lending to sub-investment grade borrowers or other types of private credit funds, such as liquid credit funds.⁹¹

‘Originate to distribute’—the growth of securitisation

49. As set out above, the cost of bank lending has increased, resulting in banks retreating from certain types of riskier lending. In response to this, banks are further increasing their reliance on securitisation as a tool for capital management. Dr Narine Lalafaryan told us that banks “are now in the business of originating debt and then selling it to the secondary market”,⁹² and added that, for corporate loans, a bank’s “primary concern is what is going to happen to me if I do not manage to offload this debt, [...] when there will be lots of costs imposed on a bank as a result.”⁹³
50. Whilst securitisation is not new, this market is commercially beneficial for both banks and non-banks, including private credit. Michael Roberts told us that securitisation is “a good way for the banking system to actively manage its loan portfolio so that we keep excessive risk out of the banking system”,⁹⁴ and that HSBC uses “those [private credit] funds to take a lot of our exposures that are not suited for the banking system.”⁹⁵ The FCA told us that the non-banks, including private credit funds, “tend to rely more heavily on securitisation for funding in the absence of other funding sources such as

87 Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

88 Supplementary written evidence from the Bank of England ([PMG0043](#))

89 *Ibid.*

90 *Ibid.*

91 Liquid credit funds are a form of private credit which invest in publicly traded bonds.

92 [Q 19](#) (Dr Narine Lalafaryan)

93 [Q 20](#) (Dr Narine Lalafaryan)

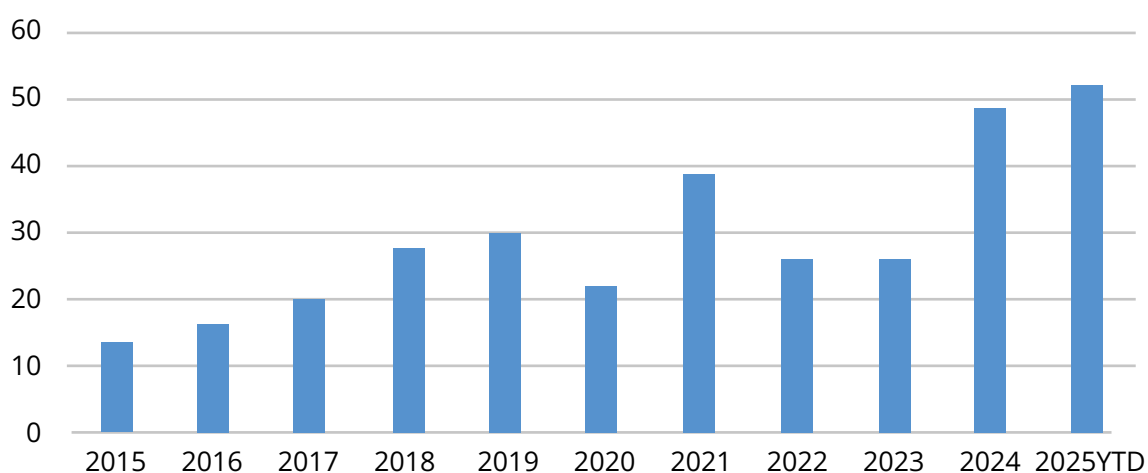
94 [Q 172](#) (Michael Roberts)

95 [Q 168](#) (Michael Roberts)

retail deposits.”⁹⁶ The evidence pointed to collateralised loan obligations and significant risk transfers as important and growing forms of securitisation.

51. Witnesses from Barclays and HSBC noted that both banks use collateralised loan obligations,⁹⁷ which are made up of multiple loans held by a company specifically created for this purpose (a special purpose vehicle). Investors can buy securities issued by this company, which entitles them to a share of the repayments on the loans it holds. David Postings estimated that there is approximately £450 billion in outstanding collateralised loan obligations.⁹⁸ Noting that two-thirds of European collateralised loan obligation managers are based in the UK, FCA data indicate that this market has grown significantly over the past decade.⁹⁹

Figure 2: Issuance of collateralised loan obligations in the European market (inc. the UK) [EUR billion]



Source: Written evidence from the FCA ([PMG0040](#)), Bank of America Global Research

52. Although typically associated with bank lending, we received some evidence to indicate that a market for securitising private credit is emerging. The Loan Market Association highlighted that the US private credit securitisation market is the most developed globally, with \$41.77 billion of securities issued in 2024, or 19.6% of total collateralised loan obligation issuance.¹⁰⁰ Contrastingly, the Loan Market Association was aware of only two issuances of private credit collateralised loan obligations in Europe at the time of submission, and expected the growth in Europe and the UK to be more subdued than the US.¹⁰¹
53. We were told by the FCA that banks use significant risk transfers to manage risk on their balance sheet by “selling a sufficient portion of riskier first or second loss tranche(s) of the securitisation to external investors, e.g. through Credit-Linked Notes, while retaining the less risky senior tranches.”¹⁰² A

96 Written evidence from the Financial Conduct Authority ([PMG0040](#))

97 [Q 172](#) (Michael Roberts); [Q 172](#) (Stephen Dainton)

98 [Q 95](#) (David Postings)

99 Written evidence from the Financial Conduct Authority ([PMG0040](#))

100 Written evidence from the Loan Market Association ([PMG0029](#))

101 *Ibid.*: “Barings launched the first European middle market private credit CLO (€380 million) in November 2024, followed by Ares Management Corporation’s European Direct Lending CLO (£305 million) in June 2025.”

102 Written evidence from the Financial Conduct Authority ([PMG0040](#))

significant risk transfer transfers a substantial part of the credit risk associated with an asset [loan], whilst retaining the asset on the issuer’s balance sheet. Consequently, the issuing bank can reduce correspondingly the amount of risk weighted capital it is required to hold. The Loan Market Association highlighted that significant risk transfers have developed in the UK and Europe in anticipation of an increase in capital requirements under the Basel 3.1 bank capital requirements.¹⁰³ Moreover, the Loan Market Association noted that private credit has emerged as a significant investor into significant risk transfers.¹⁰⁴

54. The FCA noted that the UK’s securitisation market, whilst considerably smaller than in 2006–2008, has grown consistently since 2015 to £180 billion in outstanding public securitisations in September 2025, excluding collateralised loan obligations.¹⁰⁵
55. When discussing the collapse of First Brands and Tricolor, Andrew Bailey noted that: “We are certainly beginning to see, for instance, what used to be called slicing, dicing and tranching of loan structures going on. If you were involved before the financial crisis and during it, alarm bells start going off at that point.”¹⁰⁶
56. **The growth in collateralised loan obligations and significant risk transfers in the UK may pose a potential risk to the UK’s financial stability. The Bank of England and the Prudential Regulation Authority should pay close attention to the development of these markets.**

Diversification in the UK’s debt market

57. Several witnesses highlighted the benefits of diversifying the sources of debt that the UK economy can secure. Nathanaël Benjamin, Executive Director for Financial Stability Strategy and Risk at the Bank of England, told us that: “It is a good thing for the economy to have different parts of the financial system providing different parts of lending, and for the lending to come from the bits of the financial sector that are best placed to provide it.”¹⁰⁷
58. Co-lending between banks and private credit appears to be increasing, which leverages each sector’s respective advantages. The Loan Market Association shared market analysis which suggested that “the number of deals involving bank-led senior debt and fund-led junior instruments is increasing”.¹⁰⁸ Daniel Leiter suggested that banks are lending more to private credit funds rather than directly to borrowers because “it is more attractive for them to do that from a returns and risk perspective than to make the loans directly”.¹⁰⁹
59. Apostolos Gkoutzinis, Partner in Corporate Finance, Securities and Leveraged Finance at Milbank LLP, illustrated how this cooperation works

103 Written evidence from the Loan Market Association ([PMG0029](#)). The Basel 3.1 standards are the elements of the Basel III Framework, developed in response to the Global Financial Crisis, yet to be implemented in the UK. See: Prudential Regulation Authority, *PS9/24—Implementation of the Basel 3.1 standards near-final part 2*, September 2024, pp 7–8

104 Written evidence from the Loan Market Association ([PMG0029](#))

105 Written evidence from the Financial Conduct Authority ([PMG0040](#))

106 [Q 109](#) (Andrew Bailey)

107 [Q 152](#) (Nathanaël Benjamin). See also: Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

108 Written evidence from the Loan Market Association ([PMG0029](#))

109 [Q 135](#) (Daniel Leiter)

in practice: banks may provide loans “on a secure, first-priority basis”¹¹⁰, the borrower may also require “additional financing on a subordinated basis, which is a little riskier, but more lucrative on a risk-reward basis. The direct lenders will come and take that position.”¹¹¹

60. Complementary lending provides a more diverse range of debt financing to support long-term funding for the real economy, such as for infrastructure projects. Michael Roberts told us that: “A long tenured loan of that nature is, frankly, too expensive for us to hold in our own balance sheet”.¹¹² Echoing this, Tristram Leach, Partner and Co-Head of European Credit at Apollo Global Management, noted that the “long-dated nature of the capital [provided by private credit] acts as a good counterpart for banks, which tend to be best at providing shorter-dated financing.”¹¹³
61. Conversely, banks can supplement private markets by providing debt finance or services that private markets either cannot, or typically do not, offer. Charlie Nunn highlighted that there are certain types of lending that “non-banks do not do, whether it is SMEs, working capital, revolving credit facilities or development finance.”¹¹⁴ He added: “We facilitate payments and cash management. We do all the risk management around inflation rates and FX [Foreign Exchange]”.¹¹⁵
62. The Loan Market Association suggested that this demonstrates the complementary position of banks and private credit lenders: “Private credit (for the most part) is unable to provide working capital and ancillary facilities, meaning that in all direct lending transactions, the capital structure will feature a bank-provided revolving credit facility”.¹¹⁶

A more competitive debt market

63. The evidence indicated that the growth of private credit has increased competition in the UK’s corporate debt market. According to the European Leveraged Finance Association, private credit’s “expansion has contributed to a more diverse and competitive lending environment, which benefits borrowers through improved pricing, greater flexibility, and tailored capital solutions.”¹¹⁷ Similarly, the Bank of England acknowledged that the growth in private markets “has broadened the types of capital available to the real economy, bringing benefits from greater competition and diversification.”¹¹⁸
64. Moreover, the Association for Financial Markets in Europe told us that as “private credit funds have expanded their operations, through larger deals and by moving into the investment grade space, competition between banks and private credit funds has increased.”¹¹⁹ Apostolos Gkoutzidis highlighted that this extends to competition for talent; he noted this is driven by pay and “perhaps the level of rigidity, bureaucracy or the hierarchical structures that stifle individual performance within the commercial banking sector”.¹²⁰

110 [Q 74](#) (Apostolos Gkoutzidis)

111 *Ibid.*

112 [Q 168](#) (Michael Roberts)

113 [Q 131](#) (Tristram Leach)

114 [Q 143](#) (Charlie Nunn)

115 *Ibid.*

116 Written evidence from the Loan Market Association ([PMG0029](#))

117 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

118 Written evidence from the Bank of England ([PMG0021](#))

119 Written evidence from the Association for Financial Markets in Europe ([PMG0017](#))

120 [Q 74](#) (Apostolos Gkoutzidis)

65. We also received evidence that highly liquid and competitive secondary loan markets, covered in paragraphs 49 and 54, have implications for bank lending. Dr Narine Lalafaryan told us that highly liquid secondary markets place pressure on banks to think “carefully about the types of packages of debt that they are originating, because if it is not a good package, the bank might not be in a position to successfully offload the debt”,¹²¹ consequently incentivising “banks to be more involved, whether through covenant packages or through the governance side” in companies to which they lend.¹²²
66. Apostolos Gkoutzinis highlighted that competition provides a strong drive to innovate in a market that “is limited only by the imagination of these people and, of course, the regulatory standards.”¹²³ Dr Daniele D’Alvia noted that private credit has “pioneered hybrid instruments and capital structures, demonstrating remarkable agility in structuring deals that banks, constrained by standardised products and strict prudential rules, are less able to offer.”¹²⁴
67. **The UK’s corporate debt lending market is increasingly competitive as private credit steps in to fulfil demand that is underserved by banks. Concurrently, banks increasingly lend to, and are in partnership with, private credit funds. As banks have increasingly turned to an ‘originate to distribute’ model of lending, reflecting the growth of the securitisation market, these interconnections have grown.**
68. **Throughout the inquiry, we asked for data from the regulators, academics, and industry trade bodies and firms. However, we were not able to obtain extensive or detailed data on the growth of private markets in the UK, the growth of lending provided by private credit, or the scale of interconnections between banks and private markets. We are concerned that this might represent a gap in policy and rule makers’ evidence base.**
69. *The Bank of England and the Government must ensure they have a comprehensive understanding of lenders to the UK economy, specifically by identifying the proportion of (1) total corporate debt; (2) corporate debt classified by sector, provided by different funding sources, including private credit; and (3) developments in the UK’s lending ecosystem as private credit grows.*

Regulatory arbitrage?

70. Throughout the inquiry witnesses provided varying views as to whether the growth of private markets, particularly private credit, constitutes regulatory arbitrage. We understand regulatory arbitrage to be the deliberate process of “migrating [activities] to wherever oversight is less onerous.”¹²⁵ As such, the extent to which exploitation of regulatory differences accounts for the growth of private markets indicates whether this constitutes regulatory arbitrage as opposed to an organic market development.
71. Witnesses suggesting that the growth of private markets constitutes regulatory arbitrage pointed to the migration of lending from the closely

121 [Q 21](#) (Dr Narine Lalafaryan)

122 [Q 21](#) (Dr Narine Lalafaryan)

123 [Q 74](#) (Apostolos Gkoutzinis)

124 Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

125 *Ibid.*

regulated banking sector to more lightly regulated non-banks, including private markets. Dr Daniele D’Alvia told us that the 5% decline in bank lending to the real economy relative to non-banks identified by the Bank of England¹²⁶ “has in part been ‘regulatory-induced’, as tighter bank rules made credit intermediation more costly.”¹²⁷ Professor Raghavendra Rau echoed this, noting that post-2008 regulations have “created a classic opportunity for regulatory arbitrage.”¹²⁸

72. We received evidence that the regulatory regime directly incentivises banks to lend to private markets rather than directly to companies. As noted in paragraph 27, Michael Roberts told us that a typical bank loan to a private credit fund would be weighted at 20% compared to 100% for a corporate loan because “the way that you lend into private credit is based on a secured basis that gets certain preferable treatment under the Basel regimes, so that becomes a less capital consumptive form of lending.”¹²⁹
73. Conversely, several witnesses emphasised that the relative stringency of banking regulation reflects their unique position in the financial system. Charlie Nunn pointed out that: “Banks are uniquely able to create trust in deposits while channelling deposits into the real economy as lending so that people can buy homes and businesses can grow.”¹³⁰ Professor Simon Gleeson told us that regulation is not intended to confer an advantage on private markets:

“We regulate banks not because they lend but because they take deposits; they are the gateways to the payment system and all the rest of it. It might be more accurate to say that the regulatory system places regulated banks under some slight disabilities by reason of the fact that they are licensed to raise deposits, that being their unique privilege and something that no one else has.”¹³¹

74. Andrew Bailey said:

“I would argue very strongly that that is not the purpose of the regulated system. The purpose of the regulatory system is on the liabilities side. [...] The core point about the liability of the banking system is that the nominal value of the money in the bank—of the deposits—is assured. [...] That lies at the heart of why we regulate the banking system differently, in my view.”¹³²

75. This suggests that the regulatory regime confers significant advantages on banks, notably by allowing them to fund their operations at “very low cost”¹³³ using deposits, and imposes commensurate safeguards through deposit protection and access to central bank liquidity.¹³⁴ Private credit, lacking both the benefits and regulation of banks, does not have an absolute competitive advantage, rather its funding structure makes it better placed to

126 Written evidence from the Bank of England ([PMG0021](#))

127 Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

128 Written evidence from Professor Raghavendra Rau ([PMG0036](#))

129 [Q 165](#) (Michael Roberts)

130 [Q 141](#) (Charlie Nunn)

131 [Q 4](#) (Professor Simon Gleeson)

132 [Q 107](#) (Andrew Bailey)

133 Written evidence from the Investment Association ([PMG0013](#))

134 Written evidence from Professor Vincenzo Bavoso ([PMG0004](#)); [Q 63](#) (Lord King of Lothbury)

originate certain types of corporate loans for which demand has increased.¹³⁵ Indeed, we received evidence that it is private credit's inherent advantages which make it attractive to businesses, rather than lower cost facilitated by regulatory arbitrage. Professor Ludovic Phalippou told us that in an exercise in which a bank and private credit fund both negotiated a simulated debt package, those acting in the place of the company "went for the private credit fund. They were more expensive, but they went for the private credit fund anyway."¹³⁶

76. **The differences in the regulation—particularly capital and liquidity regulatory requirements—between the banking system (which creates money) and private credit (which does not) have led to the migration of certain types of lending from banks to private credit funds, as was intended.**

135 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

136 [Q 19](#) (Professor Ludovic Phalippou)

CHAPTER 3: SME LENDING

77. SMEs are crucial to the UK economy, employing 16.9 million people, 60% of the private sector workforce, and generating an annual turnover of £2.8 trillion.¹³⁷ SMEs are an important contributor to the UK economy and its future growth, as we set out in our previous report;¹³⁸ therefore it is vital that regulation facilitates the provision of finance to meet the funding needs of SMEs. Whilst we recognise the importance of equity finance to growing companies, as noted in our previous report,¹³⁹ our focus in this inquiry has been on the development of the SME lending landscape, reflecting the predominance of debt finance.
78. SMEs are businesses with at least two of a turnover of less than £54 million, a balance sheet of less than £27 million, and fewer than 250 employees.¹⁴⁰ As such, the SME population is diverse, encompassing businesses ranging from sole operators to rapidly scaling mid-market firms.¹⁴¹ In 2025, 99.18% of the total business population, 5.64 million companies, were small businesses with fewer than 50 employees; 38,435 UK businesses were medium-sized with between 50–249 employees, 0.67% of the total business population.¹⁴²

The SME finance landscape

79. Martin McTague OBE, Chair of the Federation of Small Businesses, told us that “The UK SME market is dominated by debt. At the last count, 98% of external finance was debt and only 2% was equity.”¹⁴³ Whilst the UK’s 34,000 rapidly growing scale-up SMEs, those with annual headcount or turnover growth of greater than 20%,¹⁴⁴ use a more diverse blend of “debt and working capital, as well as equity”,¹⁴⁵ the evidence indicated a strong preference for debt finance across SMEs of all types.
80. Witnesses told us that this preference for debt finance reflects SME owners’ reluctance to seek equity finance, in which an investor provides capital in exchange for shares of ownership in a company. Professor Simon Gleeson suggested that this is due to owners’ desire “to maintain ownership of the whole damn thing. It is yours. You built it; why would you give it away?”¹⁴⁶ Additionally, Nigel Terrington suggested that “debt finance is cheaper than equity” and questioned the availability of private equity “to the micro-end of the market” suggesting that maybe there may be “a gap in the system that would need to be facilitated”.¹⁴⁷ Martin McTague noted that equity investors

137 Department for Business and Trade, *Business population estimates for the UK and regions 2025: statistical release*, October 2025

138 Financial Services Regulation Committee, *Growing Pains: Clarity and Culture Change Required. An examination of the secondary international competitiveness and growth objective* (2nd report, Session 2024–25, HL Paper 133), pp 65–67

139 Financial Services Regulation Committee, *Growing Pains: Clarity and Culture Change Required. An examination of the secondary international competitiveness and growth objective* (2nd report, Session 2024–25, HL Paper 133), pp 89–90

140 Companies Act 2006, [section 465](#)

141 [Q 58](#) (Martin McTague OBE); [Q 48](#) (Irene Graham OBE)

142 Department for Business and Trade, *Business population estimates for the UK and regions 2025: statistical release*, October 2025

143 [Q 48](#) (Martin McTague OBE)

144 [Q 48](#) (Irene Graham OBE)

145 *Ibid.*

146 [Q 11](#) (Professor Simon Gleeson)

147 [Q 90](#) (Nigel Terrington)

typically “will want 20% return a year. They want their money back in five years.”¹⁴⁸

SME lending since 2008

81. The evidence indicated that bank lending, including lending to SMEs, declined following the Global Financial Crisis. Andrew Bailey told us that “we saw a shift away from bank financing of SMEs in the aftermath of the financial crisis.”¹⁴⁹ Charlie Nunn explained that following 2008, borrowers, lenders, and SMEs “were deleveraging, they had overextended themselves and the economy was very difficult.”¹⁵⁰ The Bank of England’s data corroborated this: “The absolute amount of UK corporate debt troughed in 2014, around 10% below its 2008 peak [...] While the amount of market-based debt continued to increase steadily during this time, bank provided loans contracted by over one-third.”¹⁵¹
82. Whilst the Bank of England noted that UK corporate debt increased 35% from 2014 to £1.3 trillion by 2019,¹⁵² witnesses suggested that the recovery of debt finance was uneven. Martin McTague highlighted analysis by Allica Bank¹⁵³ which found that SME lending is “£65 billion short of where we were prior to the financial crisis.”¹⁵⁴

The importance of smaller and specialist banks in SME lending

83. SME lending has changed significantly since the Global Financial Crisis, with smaller and specialist banks providing a majority of SME lending. Louis Taylor CBE, Chief Executive Officer of the British Business Bank, told us that “60% of lending to small businesses comes from outside of the big five banks.”¹⁵⁵ Analysis from the British Business Bank indicated that in 2025 the UK’s five largest banks provided 40% of total SME lending, down from 60% in 2012.¹⁵⁶ Although gross SME lending from the UK’s five largest banks remains lower in real terms in 2025 than it was in 2012,¹⁵⁷ Charlie Nunn told us that: “We are keen to lend to the SME sector. We have over £30 billion lent and broader undrawn lines this year alone. We onboarded 100,000 SMEs.”¹⁵⁸
84. Despite these developments, banks remain the main providers of credit to small businesses, as private credit is not active in this part of the market. Nigel Terrington noted that: “I do not think the private credit area is remotely interested in small lending.”¹⁵⁹ Louis Taylor explained that this was because “a [debt] fund’s structure has quite a cost to it that does not suit itself to small business lending.”¹⁶⁰

148 [Q 56](#) (Martin McTague)

149 [Q 116](#) (Andrew Bailey)

150 [Q 142](#) (Charlie Nunn)

151 Written evidence from the Bank of England ([PMG0021](#))

152 *Ibid.*

153 Allica Bank, *Rebooting SME Finance to Unlock Growth*, April 2025, pp 11–13: Allica Bank’s analysis indicated that the total stock of SME lending would be £65 billion higher had it grown at the rate seen from 1997–2004 in the period following the Global Financial Crisis.

154 [Q 48](#) (Martin McTague OBE)

155 [Q 48](#) (Louis Taylor CBE)

156 British Business Bank, *Small Business Finance Markets 2024/25*, March 2025, pp 125, 127

157 British Business Bank, *Small Business Finance Markets 2024/25*, March 2025, p 128

158 [Q 142](#) (Charlie Nunn)

159 [Q 92](#) (Nigel Terrington)

160 [Q 49](#) (Louis Taylor CBE)

The demand gap in SME lending

85. There was consensus amongst witnesses that a considerable proportion of SMEs are either underusing or not using external finance to support their growth. However, there was disagreement regarding whether this reflects limited demand for finance or an increase in the cost of credit.

Demand for SME lending

86. Much of the evidence indicated that there is limited demand for finance amongst SMEs. Citing research conducted by the Federation of Small Businesses, Martin McTague told us that “70% of survey respondents [...] would rather grow more slowly than take the risk of borrowing.”¹⁶¹ Sarah Breeden, Deputy Governor for Financial Stability at the Bank of England, told us: “We did a survey of SMEs jointly with the Department for Business and Trade. It came back with some really sobering statistics: 77% of SMEs would rather have less growth in their business than have finance, while three-quarters of them wanted to pay down debt and get to a debt-free position.”¹⁶² She added: “So it is important, as we think about these issues, to consider the demand side, financial literacy and all of those aspects, as well as the supply side [...] Perhaps it is about equity rather than debt.”¹⁶³
87. Significantly, we received evidence that a proportion of SMEs are permanently not seeking external finance. David Postings told us that: “Demand from those smaller players is weak. Forty-one per cent describe themselves as permanent non-borrowers. The SME part of the market has been a net depositor since 2012.”¹⁶⁴ Irene Graham OBE, Chief Executive Officer of the ScaleUp Institute, highlighted research conducted by BVA BRDC (now Ipsos) which shows “permanent non-borrowing”,¹⁶⁵ with 35% of SMEs neither using finance nor showing any appetite to seek external funding.¹⁶⁶
88. Witnesses emphasised that limited demand for finance primarily reflects low business confidence caused by wider economic conditions. Charlie Nunn told us that SMEs’ “costs of doing business, their costs of borrowing and their uncertainty around the economy and geopolitics are very high.”¹⁶⁷ This was echoed by Robert Begbie, Chief Executive Officer of NatWest Commercial and Institutional, who said “business appetite for leverage and risk fundamentally shifted after 2008, and subsequent shocks—Brexit, the pandemic, inflation—reinforced that cautious approach.”¹⁶⁸ Citing data from the Department for Business and Trade,¹⁶⁹ David Postings told us that of SME employers surveyed “60% cited tax, 50% energy, 44% regulation, and only 16% availability of finance”, as the main obstacle to the growth of their business.¹⁷⁰

161 [Q 55](#) (Martin McTague OBE)

162 [Q 116](#) (Sarah Breeden)

163 *Ibid.*

164 [Q 96](#) (David Postings)

165 [Q 51](#) (Irene Graham).

166 BVA BRDC, *SME Finance Monitor Q4 2024 Report*, March 2025, p 112

167 [Q 142](#) (Charlie Nunn)

168 [Q 142](#) (Robert Begbie)

169 Department for Business and Trade, *Longitudinal Small Business Survey 2024: SME employers (businesses with 1 to 249 employees)*, September 2025, section 8.1

170 [Q 96](#) (David Postings)

Constraints on SME demand

89. Although wider economic conditions are principally responsible for SMEs' limited demand for finance, the evidence indicated that a range of factors increase the difficulty of borrowing. Witnesses pointed to the decline in relationship banking, in which bank managers develop a strong understanding of local businesses and are given discretion to lend to them, as an important barrier to SMEs accessing debt finance. Handelsbanken noted: "Fundamentally, we see a number of SMEs lacking the support and advice they require, and relationship management addresses this genuine gap."¹⁷¹ A literature review by the Bank of England corroborated this, finding that a decline in relationship banking due to branch closures reduced corporate lending, particularly for smaller firms.¹⁷² Equally, citing Bank of Finland analysis of Polish bank branch structure and SME lending from 2008–2012,¹⁷³ Professor Vincenzo Bavoso from the University of Manchester Law School, told us that "the real economy, and in particular SMEs, prosper in economies characterised by networks of local banks devoted to the business of lending."¹⁷⁴
90. Significantly, relationship lenders are an important source of advice, as Nigel Terrington noted: "those small SMEs, they kind of want someone to hold their hand [...] and some help in terms of enabling them to understand what they are entering into, or what the best route through this is."¹⁷⁵ Similarly, Martin McTague highlighted that only 30% of small business loans are arranged through intermediaries, compared to 90% of mortgages, therefore "there is enormous scope for improving the availability of good advice from people who understand the market and can navigate it for small businesses."¹⁷⁶ Handelsbanken illustrated how tailored, relationship-based lending can support the needs of different businesses: "Those businesses with a focus on growth need a clear understanding of available funding options and structures, with access to liquidity. Those SMEs needing funding to mitigate cashflow pressure and deteriorating performance, need guidance and support to understand potential costs and risks."¹⁷⁷
91. The closure of bank branches has affected the availability of relationship banking, with the number of bank and building society branches falling by 40% between 2012–2022.¹⁷⁸ Andrew Bailey told us that the reduction in the number of bank branches "does leave a number of challenges in slightly different parts of our world. SME contact is one of them [...] if we cut SMEs off from what they perceive as access to banks, then that will have an effect."¹⁷⁹ However, as Nigel Terrington noted:

171 Written evidence from Handelsbanken plc (PMG0035)

172 The Bank of England, *Unlocking growth: what can the literature tell us about what's holding back high-growth firms?*, October 2025

173 Iftekhar Hasan, Krzysztof Jackowicz, Oskar Kowalewski, Łukasz Kozłowski, 'Bank Ownership Structure, SME Lending and Local Credit Markets', Bank of Finland Research Discussion Paper, No. 22/2014, Gabelli School of Business, Fordham University Research Paper No. 2851408 (2014), <https://dx.doi.org/10.2139/ssrn.2851408>

174 Written evidence from Professor Vincenzo Bavoso (PMG0004)

175 Q 91 (Nigel Terrington)

176 Q 48 (Martin McTague OBE)

177 Written evidence from Handelsbanken plc (PMG0035)

178 The Bank of England, *Unlocking growth: what can the literature tell us about what's holding back high-growth firms?*, October 2025

179 Q 119 (Andrew Bailey)

- “The withdrawal of banks from the branch system in the UK has been a journey that has been taking place over several decades, and it is not going to reverse from now. It is driven by the economics of people turning to digital banking and not using the branches. A branch is a very expensive asset, and it is no longer economic to support it.”¹⁸⁰
92. We received evidence to suggest that SME owners do not have access to the support they need when making financial decisions. Martin McTague suggested that business owners “are often driven by a passion about their particular product or service, and not by a knowledge of financial markets.”¹⁸¹ For instance, SMEs’ reliance on the UK’s five largest banks “could be because they do not have the financial literacy to make sensible choices in the market.”¹⁸² Mark Steele, Chief Risk Officer of OakNorth Bank, echoed this, suggesting that businesses’ ability to access finance “links to the education point so that SMEs can ask the right questions of their banks around the facilities that they really need to help their business”¹⁸³.
 93. The evidence indicated that a requirement to provide personal guarantees is a further barrier to SME borrowing, which 80% of Federation of Small Business members reported were required by lenders.¹⁸⁴ Martin McTague explained that “80% of SMEs are asset-light, so they do not have the security to borrow. [...] It then comes down to what available assets they have. For most small businesses, they are personal assets.”¹⁸⁵ Nigel Terrington told us that “personal guarantees are taken because that ensures you have the full faith and credit of the individual behind the small business engaged without them losing control of the ownership of their business.”¹⁸⁶ Martin McTague explained that business owners “are being asked to put their principal private residence on the line so that they can get through the next few years, that is an unacceptable risk for most small business owners to take.”¹⁸⁷ The alternative for many SMEs is not to seek external funding, and instead the “profits that you generate each year are used to fund the following year’s growth.”¹⁸⁸
 94. However, some evidence presented a more optimistic view of the SME lending market. Irene Graham told us that there “has been a lot more focus on the innovation of our banking arena, and so there is much more choice now.”¹⁸⁹ Notably, the development of new lending products may support SMEs with novel business models to access finance. Irene Graham told us that: “As we see our economy shift into tech, creative, life sciences and climate, we are seeing new products come in, whether that is IP [intellectual property] lending or recurring revenue lending.”¹⁹⁰
 95. Notably, we were told that Open Banking may facilitate innovation by increasing data sharing. Mark Steele, Chief Risk Officer at OakNorth Bank, told us that “Open Banking definitely gives banks access to further

180 [Q 91](#) (Nigel Terrington)

181 [Q 49](#) (Martin McTague OBE)

182 [Q 49](#) (Martin McTague OBE)

183 [Q 91](#) (Mark Steele)

184 [Q 48](#) (Martin McTague OBE)

185 *Ibid.*

186 [Q 90](#) (Nigel Terrington)

187 [Q 48](#) (Martin McTague OBE)

188 *Ibid.*

189 [Q 49](#) (Irene Graham OBE)

190 *Ibid.*

information and data to be able to make an appropriate credit decision.”¹⁹¹ This may give lenders greater visibility over the creditworthiness of an SME and make it easier for businesses to secure lending. Irene Graham noted that Open Banking may build on the Small Business, Enterprise and Employment Act 2015,¹⁹² which required banks and credit ratings agencies to share SMEs’ credit information.¹⁹³ She told us: “That means you can get proactively told—I get these all the time, now—‘Here are the options for you. Here are the options of the debt and their costs. Here are the options of the lending’.”¹⁹⁴

The increased cost of SME lending

96. Whilst the evidence indicated that SMEs’ underuse of finance is primarily caused by low demand, some witnesses questioned whether adequate credit is available. Louis Taylor noted that, although “demand and supply of credit are largely in balance [...] there is quite suppressed ambition for investment among businesses. Were they to become more ambitious, I do not know whether the credit providers would really be there to satisfy the demand.”¹⁹⁵ Specifically, witnesses emphasised that credit is becoming increasingly costly, as Martin McTague told us that subprime lenders, the most active participants in the SME lending market, “will typically charge up to 40% on loans, and they do only a cursory look at any kind of business plan.”¹⁹⁶ Witnesses attributed increases in the cost of lending to bank capital requirements. As Professor Simon Gleeson noted, SME lending is “economically unattractive to banks unless they can charge the sort of rates they generally cannot get away with charging”.¹⁹⁷ Witnesses identified three aspects of the regulatory regime as increasing the cost of SME lending.
97. First, as set out in paragraphs 23–31, higher capital requirements have increased the cost of capital for banks. As Charlie Nunn explained, “banks have a regulatory requirement to make sure that the cost of capital and funding is included in our pricing”,¹⁹⁸ as such, “that cost has to be ultimately passed on to our customers.”¹⁹⁹
98. Second, as set out in more detail in paragraph 111, SME lending is subject to higher risk weights, which increase the relative cost of SME lending. To mitigate this, current regulation includes an SME support factor “designed to reduce capital requirements for bank lending to [SMEs] thereby encouraging more lending to this vital sector.”²⁰⁰ Nigel Terrington explained how the SME support factor reduces the risk weight applied to SME lending: “The typical risk weight applied to SMEs is 75%, the discount factor (set at 0.7619) reduces the risk weight to c.57%.”²⁰¹ However, as Charlie Nunn noted, the SME support factor will be removed under the forthcoming Basel 3.1 regulations, which “will make it more expensive for SMEs to borrow.”²⁰²

191 [Q 91](#) (Mark Steele)

192 [Q 60](#) (Irene Graham OBE)

193 Small Business, Enterprise and Employment Act 2015, [section 4](#)

194 [Q 60](#) (Irene Graham OBE)

195 [Q 57](#) (Louis Taylor CBE)

196 [Q 51](#) (Martin McTague OBE)

197 [Q 4](#) (Professor Simon Gleeson)

198 [Q 142](#) (Charlie Nunn)

199 [Q 147](#) (Charlie Nunn)

200 Written evidence from Professor Marco Lamandini and Professor David Ramos Muñoz ([PMG0007](#))

201 Written evidence from Nigel Terrington ([PMG0041](#))

202 [Q 147](#) (Charlie Nunn)

99. In response to these concerns, the PRA has proposed to offset the removal of the SME support factor by changes to banks' other capital requirements.²⁰³ However, Nigel Terrington told us that this may only partially mitigate the removal of the SME support factor, as the new adjustment is both more complex, and may still require lenders to hold more capital in the form of the bank's own shares and retained earnings (Common Equity Tier 1 capital), which may increase the cost of lending.²⁰⁴
100. Third, as noted in paragraphs 32–33, the complexity of conduct regulation increases the cost and complexity of lending to SMEs. Charlie Nunn told us that “conduct regulation under the consumer duty applies to SMEs. [...] Our ability to invest and innovate in how we support SMEs will be compromised if we do not have that conduct certainty around SMEs.”²⁰⁵
101. **The limited use of debt finance by SMEs to fund growth primarily reflects low appetite to borrow, principally caused by low business confidence in the economy. However, the use of personal guarantees and limited access to support through advice or education have further suppressed demand.**
102. **Relationship-based lending appears to have declined in the UK, which a growing body of research suggests harms SMEs' ability to access finance when they do wish to borrow. We encourage the Government to consider how to restore access to relationship-based lending as part of its financial services strategy going forward.**
103. **The regulatory environment has made it more expensive for banks to lend to SMEs, reflecting the higher risks and costs involved in such lending. We are concerned that the commercial attractiveness of lending to SMEs may continue to decline, and that banks may reduce SME lending whilst private credit may not step in.**

The role of smaller and specialist banks in supporting SME lending

104. We received evidence that in jurisdictions with strong SME lending markets, such as the US or Germany, community banks are pivotal to ensuring that small and growing businesses can access the funding they need. Evidence we received indicated that the UK SME lending market lacks the same scale of relationship banking.²⁰⁶ Whilst we recognise that the US and German banking models cannot be directly compared with the UK's, they provide important case studies of how smaller and specialist lenders, already accounting for 60% of the SME lending market,²⁰⁷ might be enabled to better support SMEs.

203 Written evidence from Nigel Terrington ([PMG0041](#)): The PRA's proposal would offset the increase to banks' core capital requirements (Pillar 1) caused by the removal of the SME support factor by a reduction in their additional capital requirements (Pillar 2A)

204 Written evidence from Nigel Terrington ([PMG0041](#)): “... its inclusion as a [Pillar 2A] offset, and not [Pillar 1], results in a higher Combined Buffer, despite total capital requirements remaining the same. Consequently, SME lending banks will need to hold more [Common Equity Tier 1] capital for the same implied level of risk, increasing the cost of capital for banks and ultimately feeding through to higher interest rates for SME borrowers and/or reduced lending capacity by banks.”

205 [Q 147](#) (Charlie Nunn)

206 [Q 51](#) (Martin McTague OBE)

207 British Business Bank, *Small Business Finance Markets 2024/25*, March 2025, pp 125, 127

Community banks in the US and Germany

105. Professor Arthur E. Wilmarth Jr., Professor Emeritus of Law at George Washington University Law School, told us that the business model of the approximately 4,000 US community banks is to build “long-term relationships with their customers and [develop] a detailed understanding of their customers’ businesses”.²⁰⁸ Community banks are central to the US SME lending market, as they “originate 70% of all agricultural loans, 36% of all small business loans, and 30% of all commercial real estate loans”, despite holding “less than 12% of U.S. banking assets.”²⁰⁹ Consequently, community banks “are widely recognized as the most engaged and reliable lenders to farmers and SMEs through the business cycle.”²¹⁰
106. Likewise, the relationship banking model of Germany’s publicly owned regional banks (Sparkassen) provides similar benefits to SMEs. Martin McTague told us that “Certainly, as far as Germany is concerned, there is significantly better availability of finance to SMEs than there is in the UK.”²¹¹ Martin McTague attributed this to Germany’s “completely different structure, which is based on regional mutuals. They are much better at assessing local regional conditions and, therefore, prepared to lend.”²¹²
107. In contrast to the relationship banking approach used by US community banks and Sparkassen, it appears that UK banks “have to move to some level of automation which creates these rules that if you are a yes, you go through to the next stage, and if you are a no, you do not.”²¹³ Echoing this, Handelsbanken observed that the UK banks utilise “more ‘mechanical’ approaches to data-led decision making, often our experience across the UK is that there is less expertise available”.²¹⁴ Nigel Terrington attributed this to the UK banking sector’s “centralised model, meaning head office determines that the type of customer that looks like this should get that rate.”²¹⁵

Constraints on UK smaller and specialist banks

108. Whilst the constraints on bank lending addressed in the previous chapter apply to smaller and specialist lenders, consistent with the findings of our previous report,²¹⁶ evidence indicated that they are disproportionately affected by the burden of compliance.
109. First, witnesses emphasised that the inability to use the internal ratings based approach to calculating risk weights disadvantages smaller and specialist banks. The internal ratings based approach allows banks to use internal credit models approved by the PRA in the process of calculating their risk weights.²¹⁷ Nigel Terrington told us that the “capital benefits of [the internal ratings based approach], while reducing due to Basel 3.1, remain

208 Written evidence from Professor Arthur Wilmarth Jr ([PMG0022](#))

209 *Ibid.*

210 *Ibid.*

211 [Q 51](#) (Martin McTague OBE)

212 *Ibid.*

213 [Q 92](#) (Mark Steele)

214 Written evidence from Handelsbanken plc ([PMG0035](#))

215 [Q 92](#) (Nigel Terrington).

216 Financial Services Regulation Committee, *Growing Pains: Clarity and Culture Change Required. An examination of the secondary international competitiveness and growth objective* (2nd report, Session 2024–25, HL Paper 133), pp 72–73

217 Bank of England, *CP16/22—Implementation of the Basel 3.1 standards: Credit risk—internal ratings-based approach*, November 2022, p 3

significant. At present this is a benefit available for only the large UK banks and building societies.”²¹⁸ Handelsbanken also emphasised the importance of the Internal Ratings Based approach, as: “Increased risk sensitivity in capital requirements could improve Handelsbanken’s ability to compete and lend more to SMEs. To achieve this, the Bank needs to adopt an [internal ratings based] approach”.²¹⁹

110. However, Nigel Terrington told us that the process to receive approval to utilise the internal ratings based approach is “quite tortuous: it is very elongated and expensive to do”.²²⁰ Handelsbanken offered the same criticism, noting that the PRA’s limited capacity to process applications to use the internal ratings based approach make it “challenging for firms to establish the PRA’s modelling expectations”, adding that “medium-sized firms [...] often lack volume of historical data—especially default and loss data—which makes it harder to meet PRA modelling expectations.”²²¹ Whilst both welcomed recent proposals by the PRA to simplify and accelerate the process of gaining permission to utilise the internal ratings based approach,²²² Nigel Terrington noted that “it is unclear how long the PRA will take to move from discussion points to implemented policy”.²²³
111. Second, Nigel Terrington told us that the risk weights on SME lending “will probably be twice the level of mortgages; corporates will be three times the level; and housebuilders, which is around five times the level”.²²⁴ David Postings told us that, under the standardised approach used by challenger banks, the typical risk weights for a £100,000 business loan to an SME are 55%, while they are 31% for a high street bank operating under the internal ratings-based model.²²⁵ Conversely, he stated that the risk weights on a £100,000 75% loan-to-value mortgage are notably lower, at 35% for a challenger bank and 17% for a high street bank.²²⁶
112. Moreover, witnesses emphasised that the risk weights do not capture the risks of a specific loan, as Lord King of Lothbury noted: “Branding them all with a high-risk label and a high risk weight is not going to help create an environment in which people can say, ‘There is a profitable opportunity here’.”²²⁷ Similarly, Mark Steele highlighted that the risk weights do not reflect the due diligence that a smaller or specialist lender performs when lending: “we are looking at the interest cover, the [Loan to Value] ratio, the sponsor, the levels of equity, their past performance and our projections for the future, none of which is reflected in static risk weights.”²²⁸
113. **Although smaller and specialist lenders have become increasingly important to the UK SME lending market, regulation continues to constrain their capacity to lend to SMEs. We encourage the Government and the Bank of England to explore what lessons might**

218 Written evidence from Nigel Terrington ([PMG0041](#))

219 Written evidence from Handelsbanken plc ([PMG0035](#))

220 [Q 87](#) (Nigel Terrington)

221 Written evidence from Handelsbanken plc ([PMG0035](#))

222 [Q 94](#) (Nigel Terrington); Written evidence from Handelsbanken plc ([PMG0035](#))

223 Written evidence from Nigel Terrington ([PMG0041](#))

224 [Q 85](#) (Nigel Terrington)

225 [Q 96](#) (David Postings)

226 [Q 98](#) (David Postings)

227 [Q 72](#) (Lord King of Lothbury)

228 [Q 83](#) (Mark Steele)

be learnt from the regulation of community banking sectors in the US and Germany.

114. **Whilst the Committee welcomes the Financial Policy Committee's reduction in the appropriate benchmark for the system-wide level for capital requirement, this does not substantively address long-standing concerns with the disproportionate application of the UK's capital and liquidity regulatory regime. Modifying the regulatory constraints on smaller and specialist lenders could help these lenders to grow and they in turn would be better positioned to increase their SME lending.**
115. *We welcome the Financial Policy Committee's announcement that it will review several aspects of the capital regime and hope that this can be completed rapidly. The PRA should implement any changes in a way which maximises the amount of bank capital which can be made available to support lending, including to SMEs. The Prudential Regulation Authority should move quickly to implement its proposed changes to the IRB approval process and risk weightings of assets.*

CHAPTER 4: FINANCIAL STABILITY

116. As noted in paragraphs 7–8, the Bank of England has begun to look more closely at the implications that the growth of private markets might have on the UK’s financial stability. The Financial Policy Committee’s July 2025 Financial Stability Report stated that it is increasing its focus on the potential system-wide vulnerabilities and contagion risks from private markets; in particular, this report raised concerns about vulnerabilities relating to private markets from high levels of leverage, opacity around valuations, and interconnectedness with other parts of the financial system.²²⁹
117. As noted in paragraphs 15–20, private credit and private equity are playing an increasingly significant role in the UK economy. Therefore, a key question we sought to examine was whether the growth of private credit and private equity markets poses risks to financial stability; and whether the interconnections between banks and private markets could be a source of systemic risk. On these issues, the evidence was mixed.

Definitions of financial stability and systemic risk

118. The Bank of England Act 1998 placed a “Financial Stability Objective”²³⁰ on the Bank of England, to protect and enhance the stability of the UK’s financial system. Financial stability is defined as ensuring that the financial system “has sufficient resilience to be able to facilitate and supply vital services by financial institutions, markets and market infrastructure to households and businesses, in a manner that absorbs rather than amplifies shocks.”²³¹ The vital financial services without which the UK’s economy would not function are:²³²
- (a) Payment and settlement services, meaning that bank transfers, card payments, and online payments function.
 - (b) Intermediating between savers and borrowers, meaning that customers can continue to access their deposits, including current and savings accounts, and that banks continue to provide credit to the economy.
 - (c) Insuring against and dispersing risk, meaning that the financial impact of negative events can be shared so it does not fall on one individual or company.
119. The Bank of England Act 1998 defines systemic risk as “a risk to the stability of the UK financial system as a whole or of a significant part of that system”,²³³ which can arise in the UK or overseas.²³⁴ A firm or sector can be considered systemic once it is significant enough to pose a risk to the provision of vital financial services, that is financial stability, in the event of disruption, such as the collapse of a firm or contraction in economic activity. The legislation identifies three key causes of systemic risk: the structure of financial markets, particularly connections between financial institutions; the distribution of

229 Bank of England Financial Policy Committee, *Financial Stability Report, July 2025*

230 Bank of England Act 1998, [section 2A](#)

231 Bank of England, *The Bank’s Financial Stability Strategy*, last updated 17 November 2023

232 *Ibid.*

233 Bank of England Act 1998, [section 9C](#)

234 Bank of England, *The contribution of the Financial Policy Committee to UK financial stability*, September 2024

risk within the financial sector; and unsustainable levels of leverage, debt, or credit growth.²³⁵

120. Following the Global Financial Crisis, national and international regulators adopted the concept of a ‘Global Systemically Important Financial Institution’ (G-SIFI)²³⁶ to identify firms whose failure would pose a systemic risk. Factors indicating that a firm may be significant enough to pose a systemic risk include: size, scale, complexity, concentration, leverage, opacity, the extent of interconnections with systemic parts of the financial system (such as banks), cross border activity, and importance to a particular sector, region, or the system at large.²³⁷ Many of these factors were referred to within our evidence.

Does the UK’s private credit market pose a systemic risk?

121. We received some evidence indicating that the structure of private credit and private equity funds mitigates systemic risk. TheCityUK told us that these funds are “closed-ended and funded by long-term investors with no redemption rights; therefore, capital is locked in, preventing market-wide implications.”²³⁸ The Loan Market Association echoed this, suggesting that the ability of private credit to impact financial stability might be limited by the FCA’s proposed reforms to the Alternative Investment Fund Managers regulatory regime.²³⁹ They told us that this will require Loan Originating Alternative Investment Fund managers to be closed-ended funds, “unless the manager can demonstrate that the AIF’s [Alternative Investment Fund] liquidity risk management system is compatible with its investment strategy and redemption policy.”²⁴⁰
122. We also received evidence to suggest that private credit has pushed activity away from the banking system by, as suggested by Professor Simon Gleeson, “squeezing the riskier part of the business out of the banking system and into the non-banking system”.²⁴¹ Similarly, the Investment Association told us that private credit can mitigate risks to financial stability by “[dispersing] any risk of loss from private credit loans away from the banking system, reducing risk exposures of taxpayers and retail depositors with private credit funds’ downside risks borne solely by their global base of highly sophisticated private investors.”²⁴²

235 Bank of England Act 1998, [section 9C](#)

236 Financial Stability Board, [Globally Systemically Important Financial Institutions \(G-SIFIs\)](#), updated 27 November 2025

237 Rosa M. Lastra, “Systemic Risk, SIFIs and Financial Stability,” *Capital Markets Law Journal*, Vol. 6, No. 2, April 2011, pp 197–213: <https://doi.org/10.1093/cmlj/kmr009>; Rosa M. Lastra, *International Financial and Monetary Law* (Oxford University Press, 2015), Chapter 4

238 Written evidence from TheCityUK ([PMG0009](#)). A closed-end fund raises capital that is committed for a pre-agreed period during which investors are not able to withdraw their capital. Conversely, an open-ended fund allows investors to commit capital, or redeem their investment, throughout the life of the fund.

239 At the time of publication, HM Treasury and the Financial Conduct Authority are consulting in parallel on the introduction of a new legal and regulatory framework for the Alternative Investment Fund Managers Directive. See: HM Treasury, [Alternative Investment Fund Managers Regulations consultation](#), April 2025; Financial Conduct Authority, [Call for Input: Future regulation of alternative fund managers](#), April 2025

240 Written evidence from the Loan Market Association ([PMG0029](#))

241 [Q 7](#) (Professor Simon Gleeson)

242 Written evidence from the Investment Association ([PMG0013](#))

123. The majority of investors into private credit and private equity funds appear to be sophisticated, institutional, and internationally based. The Managed Funds Association explained:

“The investors in these funds are usually sophisticated, often institutional, investors such as pension funds, insurance companies, sovereign wealth funds, endowments, and high-net-worth individuals. The funds have a long-term funding structure and originate loans with an intention to hold them to maturity.”²⁴³

This, they explained, differs from bank depositors, who can withdraw money from their accounts at any time. The commitment from sophisticated investors to multi-year holding periods “prevents runs on a private credit fund and provides long-term stability to borrowers and other investors.”²⁴⁴

124. Several witnesses challenged the suggestion that the growth of private credit and private equity posed risks for financial stability. The Managed Funds Association highlighted that: “Private credit funds [...] are not backed, insured, or guaranteed by the government. Taxpayer money is therefore not at risk in times of fund stress.”²⁴⁵ The British Venture Capital & Private Equity Association echoed this: “from a financial stability perspective, private capital funds do not exhibit the transmission channels commonly associated with systemic instability.”²⁴⁶

What features of private credit markets are causing concern?

125. As set out previously private markets are an increasingly important provider of long-term finance to the real economy. The Bank of England stated that private markets have “expanded not only in size but also in complexity and interconnectedness.”²⁴⁷ Many of our witnesses suggested that with this growth, any inherent vulnerabilities may increase as well.
126. The potential risks in private markets have been examined by national and international regulators.²⁴⁸ As noted in paragraph 8, the failure of First Brands and Tricolor has increased regulatory scrutiny of these risks. The evidence we received broadly was in line with the findings of the Financial Policy Committee²⁴⁹, and highlighted the potential risks caused by valuations, the use of leverage, and a possible decline in underwriting standards due to the increasing competitiveness of the market.

Valuations

127. Valuations in private markets differ substantially from valuations in public markets, reflecting “the very different structural nature of private markets as compared to public markets.”²⁵⁰ Unlike public markets in which “valuations are driven by observable market price”,²⁵¹ in private markets valuations “are typically done quarterly or at transaction events, based on models or

243 Written evidence from the Managed Funds Association ([PMG0012](#))

244 *Ibid.*

245 *Ibid.*

246 Written evidence from the British Venture Capital & Private Equity Association ([PMG0016](#))

247 Written evidence from the Bank of England ([PMG0021](#))

248 Bank of England, *Financial Stability Report July 2025*, July 2025, pp 85–90; *Financial Stability Board, Leverage in Nonbank Financial Intermediation: Final report*, July 2025, pp 4–5

249 Written evidence from the Bank of England ([PMG0021](#))

250 Written evidence from the Investment Association ([PMG0013](#))

251 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

comparable company multiples.”²⁵² The FCA, which regulates many private market firms, found that 98.47% of private equity firms produce quarterly valuations of portfolio companies.²⁵³ The Investment Association suggested that quarterly valuations “means reported values move slowly and may not immediately reflect market conditions.”²⁵⁴

Risks relating to private credit and private equity market valuations

128. Isolated instances of inaccurate valuations have implications for investor protection²⁵⁵ and, if widespread, this could “become a particular issue in any period of stress if confidence in valuations is lost.”²⁵⁶ Professor Marco Lamandini, Professor of Commercial Law at the University of Bologna, and Professor David Ramos Muñoz, Associate Professor of Commercial Law at Universidad Carlos III de Madrid, explained that inaccurate valuations may lead to “rapid price corrections”.²⁵⁷ Witnesses highlighted three potential risks in private market valuations.
129. First, witnesses raised concerns regarding the accuracy of private market valuations. Professor Ludovic Phalippou told us that valuations “are off in private credit because of a massive increase in interest rates, and then we do not see much default, despite the fact that the cost of debt has doubled on average.”²⁵⁸ Echoing concerns raised by the IMF,²⁵⁹ he suggested that higher interest rates have not led to increased defaults, as private credit lenders have been able to renegotiate the terms of the loan to prevent default.²⁶⁰
130. Second, potential conflicts of interest can affect the accuracy of private market valuations. In March, the FCA published its findings of its multi-firm review of valuation practices for private market assets. The review “assessed the robustness of firms’ valuation processes and governance arrangements, including the checks and balances that help address the risk of poor conduct and harm to investors.”²⁶¹ The findings identified firms’ management fees as such a potential conflict of interest.²⁶² The British Venture Capital & Private Equity Association claimed that management fees depend on the amount of capital committed, not the value of the fund, “so private capital firms do not generally get higher fees if they report a higher interim valuation.”²⁶³ However, the FCA found that a decrease in a fund’s valuation “represented a decrease in the value of invested capital and reduced management fees.”²⁶⁴ This “could dissuade [fund managers] from taking appropriate write-downs to avoid lost management fees.”²⁶⁵

252 Written evidence from the Investment Association (PMG0013)

253 Written evidence from the Financial Conduct Authority (PMG0040)

254 Written evidence from the Investment Association (PMG0013)

255 Written evidence from the Financial Conduct Authority (PMG0040)

256 Written evidence from the Bank of England (PMG0021)

257 Written evidence from Professor Marco Lamandini and Professor David Ramos Muñoz (PMG0007)

258 Q 22 (Professor Ludovic Phalippou)

259 International Monetary Fund, *Global Financial Stability Report, April 2024*, April 2024, p 59: “The rise in benchmark rates has increased the interest burden for private credit borrowers, prompting some firms to resort to payment-in-kind interest. This flexibility may help borrowers withstand temporary stress, but it can lead to compounding losses if a firm’s underperformance cannot be reversed.”

260 Q 22 (Professor Ludovic Phalippou)

261 Written evidence from the Financial Conduct Authority (PMG0040)

262 Financial Conduct Authority, *Multi-Firm Review: Private Market Valuation Practices*, March 2025, section 2.2

263 Written evidence from the British Venture Capital & Private Equity Association (PMG0016)

264 Financial Conduct Authority, *Multi-Firm Review: Private Market Valuation Practices*, March 2025, section 2.2

265 *Ibid.*

131. Equally, conflicts of interest may occur when private market participants seek bank financing. Sheila Bair, Former Chair of the Federal Deposit Insurance Corporation, explained that for US banks to benefit from the lower risk weights on lending to private market funds (as referred to in paragraph 27), they “require that the loans be significantly overcollateralized” and that “the fund itself assigns collateral values”.²⁶⁶ Similarly, the FCA found that in loans secured against a fund’s portfolio of assets “common covenants include a minimum level of diversification within the portfolio and a maximum loan-to-value ratio”, which introduces a potential conflict of interest as “valuations could be inflated to attract a greater amount of initial borrowing or avoid breaching an [loan-to-value] LTV covenant.”²⁶⁷
132. Third, witnesses expressed concerns regarding the use of third-party rating agencies in private markets. Nathanaël Benjamin noted that credit ratings are typically used “directly for private equity, for example, for acquisition financing”²⁶⁸ and in private credit “when collateralised loan obligations are backed by private loans and when there is a demand for ratings of those [collateralised loan obligations].”²⁶⁹ Nathanaël Benjamin raised concerns about the accuracy of certain credit ratings: “There have been questions asked about those private ratings and the extent to which they can be optimistic in comparison with the ratings of the bigger agencies.”²⁷⁰ The accuracy of credit ratings has been brought into focus by failures in the US. Andrew Bailey told us that, when speaking with people from private credit and private equity: “Of course, they told me that everything was fine in their world, apart from the role of the rating agencies. I said, ‘We are not playing that movie again, are we?’”²⁷¹

Leverage

133. We received some evidence regarding the presence of leverage throughout private credit and private equity markets. The Financial Stability Board explained that “the build-up of leverage creates a vulnerability that, when subject to a shock, can propagate strains through the financial system, amplify stress, and lead to systemic disruption”.²⁷² Lord King put this directly: “Excessive leverage has always been the common theme in past financial crises.”²⁷³ Evidence from the Bank of England indicated that leverage is present throughout private markets, with private equity and private credit funds exposed to leverage as well as the companies they invest in and lend to.²⁷⁴

Risks relating to leverage

134. Professor Ludovic Phalippou described how “private credit funds often borrow themselves in order to lend, so have layer after layer of leverage.”²⁷⁵ Such leverage is often provided by banks through loans secured against a

266 Written evidence from Sheila Bair ([PMG0026](#))

267 Financial Conduct Authority, *Multi-Firm Review: Private Market Valuation Practices*, March 2025, section 2.2

268 [Q 159](#) (Nathanaël Benjamin)

269 *Ibid.*

270 *Ibid.*

271 [Q 109](#) (Andrew Bailey)

272 Financial Stability Board, *Leverage in Nonbank Financial Intermediation: Final report*, July 2025, p 5

273 [Q 71](#) (Lord King of Lothbury)

274 Written evidence from the Bank of England ([PMG0021](#))

275 [Q 25](#) (Professor Ludovic Phalippou)

fund's net asset value.²⁷⁶ As the Bank of England noted: “These facilities enable funds to increase their leverage and introduce what is often referred to as ‘leverage on leverage’, amplifying both potential returns and associated risks.”²⁷⁷ However, witnesses emphasised that leverage at the fund level is limited, particularly in private credit. Daniel Leiter told us that: “Where leverage in our funds is used, it is typically up to £1 of borrowing for £1 of investor capital, compared with banks, which often borrow more than £10 for £1 of their own capital.”²⁷⁸ Nathanaël Benjamin echoed this, noting that “the extent of leverage of individual [private finance] funds tends to be moderate, say 50% loan-to-value.”²⁷⁹

135. However, Ignazio Angeloni highlighted that whilst “leverage may be limited for the immediate provider of private credit [...] it is normally greater if the entire funding chain is considered.”²⁸⁰ Nathanaël Benjamin made a similar point, noting that the central question is: “What is the full extent of leverage across all the different actors?”²⁸¹ We heard that the complex funding structures used in private credit and private equity markets make assessing the scale of leverage present in private markets challenging. Ignazio Angeloni noted that: “Lack of detailed information prevents accurate assessment of the effective leverage involved in the process leading to private credit disbursement.”²⁸² Apostolos Gkoutzinis echoed this, noting that, compared to 2008: “Some of the structures today are even more opaque, complex and sophisticated [...] There is the risk of misunderstanding risk because of complexity, lack of transparency and the absence of public financial information.”²⁸³
136. Despite the difficulties of identifying leverage in private markets, the Bank of England noted that many private equity-backed companies “have high levels of debt and are financed from riskier credit markets like leveraged loans, high yield bonds and/or [private credit] funds”.²⁸⁴

Competition and underwriting standards

137. As noted in paragraphs 63–66, the UK private credit market is highly competitive and innovative. Apostolos Gkoutzinis told us:

“Every time I say to my team, ‘This doesn’t work. We are never going to see this. It’s impossible. This is never going to work,’ two weeks later I read in internal memos that some direct lender has come up with a structure that, two weeks earlier, I was advising people was never going to work.”²⁸⁵

Risks relating to underwriting standards

138. Whilst a competitive market benefits borrowers,²⁸⁶ witnesses were concerned that the competitiveness of the private credit market may lead to less rigorous

276 Written evidence from the Bank of England ([PMG0021](#))

277 *Ibid.*

278 [Q 131](#) (Daniel Leiter)

279 [Q 159](#) (Nathanaël Benjamin)

280 Written evidence from Ignazio Angeloni ([PMG0023](#))

281 [Q 159](#) (Nathanaël Benjamin)

282 Written evidence from Ignazio Angeloni ([PMG0023](#))

283 [Q 77](#) (Apostolos Gkoutzinis)

284 Written evidence from the Bank of England ([PMG0021](#))

285 [Q 74](#) (Apostolos Gkoutzinis)

286 Written evidence from the European Leveraged Finance Association ([PMG0011](#))

underwriting standards, increasing the risk of these loans. Sarah Breeden noted that: “In the context of a competitive market, there is obviously an incentive to compete on risk management standards.”²⁸⁷ Apostolos Gkoutzinis explained: “As the funds are motivated to win business, allocate more capital and win the competition, you can imagine that they are also occasionally motivated to be more flexible in their underwriting and risk standards.”²⁸⁸ The Bank of England cited instances of weakening underwriting standards, including “the increasing share of leveraged loan deals with weaker covenants, a rise in the use of earnings add-backs to reduce headline leverage multiples, and looser documentation standards.”²⁸⁹ These concerns extend to a potential weakening of loan covenants, which require borrowers to meet conditions specified by the lender for the duration of the loan.²⁹⁰ The British Emerging Manager Institute told us that competition in the private credit market could “bring rise to the erosion of lending covenants as lenders seek to secure access to the highest credit quality borrowers.”²⁹¹

139. Witnesses from the private credit sector emphasised the rigour of their underwriting standards and risk management processes. Tristram Leach told us that “rigorous credit underwriting [...] is really the bedrock of everything we do as we search for safe yield”.²⁹² Joseph Pinto, Chief Executive Officer of Asset Management at M&G plc, told us that M&G is highly selective of the debt held by its funds: “Last year [2024], for example, we looked at 120 transactions and selected less than 10% of them. We have been extremely selective, probably because we have our own sound risk management process”.²⁹³ We recognise that we received evidence from the largest participants in the private credit market, and as such their evidence of strong underwriting standards may not be representative of practices across the sector. Apostolos Gkoutzinis noted that whilst most direct lenders “are targeting senior secured, safe, first-ranking type structures” the “minority will look into alternative structures, all the way to the distressed funds, which is a niche market in and of itself.”²⁹⁴ It is not clear whether underwriting standards in this section of the market are comparably rigorous to those of the firms from which we received evidence.

Interconnections

140. The interconnectedness between the banking sector and private market firms was cited throughout our evidence as an aspect of the financial system that requires close attention. Interconnections in the context of financial stability refers to the network of exposures and dependencies between financial institutions, markets, and infrastructures.

Why do interconnections matter?

141. The Bank of England explained that: “Interconnections across financial markets may heighten systemic vulnerabilities, particularly under stress conditions, by reinforcing correlations and amplifying shocks.”²⁹⁵ Dr Daniele

287 [Q 108](#) (Sarah Breeden)

288 [Q 74](#) (Apostolos Gkoutzinis)

289 Written evidence from the Bank of England ([PMG0021](#))

290 [Q 134](#) (Blair Jacobson)

291 Written evidence from the British Emerging Manager Institute ([PMG0001](#))

292 [Q 134](#) (Tristram Leach)

293 [Q 127](#) (Joseph Pinto)

294 [Q 79](#) (Apostolos Gkoutzinis)

295 Written evidence from the Bank of England ([PMG0021](#))

D’Alvia provided the following examples to illustrate how distress within non-bank intermediaries can reverberate into the wider financial system:

“the March 2020 Covid-19 market crash (when highly-leveraged non-bank investors had to unwind positions), the collapse of Archegos Capital Management in 2021 (a family office hedge fund whose derivatives-fuelled bets caused over \$10 [billion] of losses to global banks), and the UK ‘LDI crisis’ of September 2022 (when pension funds’ leveraged gilt investments amplified a bond sell-off)”.²⁹⁶

Interconnections between private markets and the banking sector

142. The Bank of England told us that interconnections with private markets are “pronounced”²⁹⁷ and relate to “their significant funding of the real economy; their reliance on financing from the banking sector; and their growing links with the insurance sector.”²⁹⁸ The Association for Financial Markets in Europe told us that since the Global Financial Crisis, what “began as a necessary reset of banks’ risk appetite and balance sheets has become a series of connections [with private markets] that now underpin credit formation, liquidity, and risk transfer across the system.”²⁹⁹

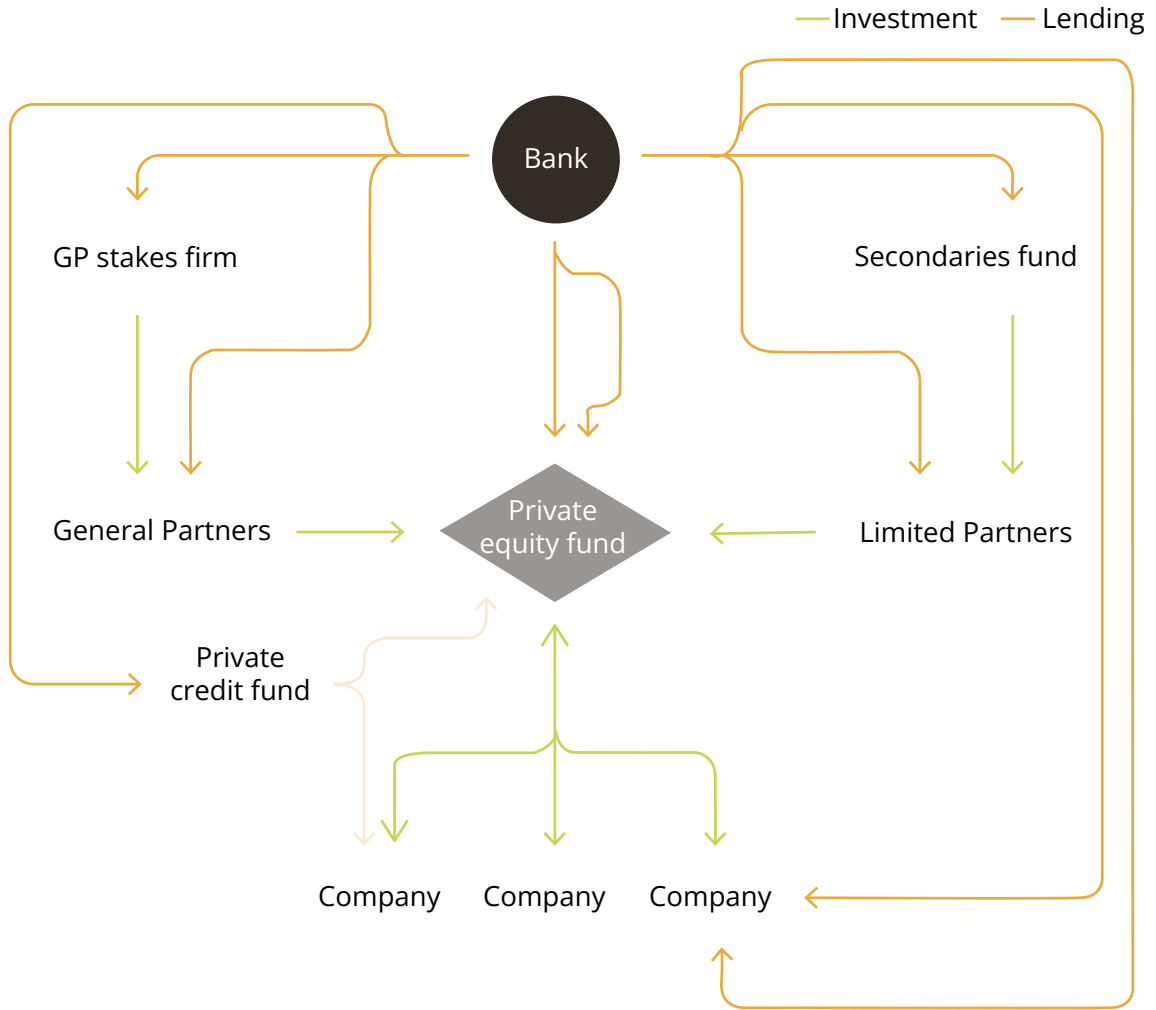
296 Written evidence from Dr Daniele D’Alvia ([PMG0008](#))

297 Written evidence from the Bank of England ([PMG0021](#))

298 *Ibid.*

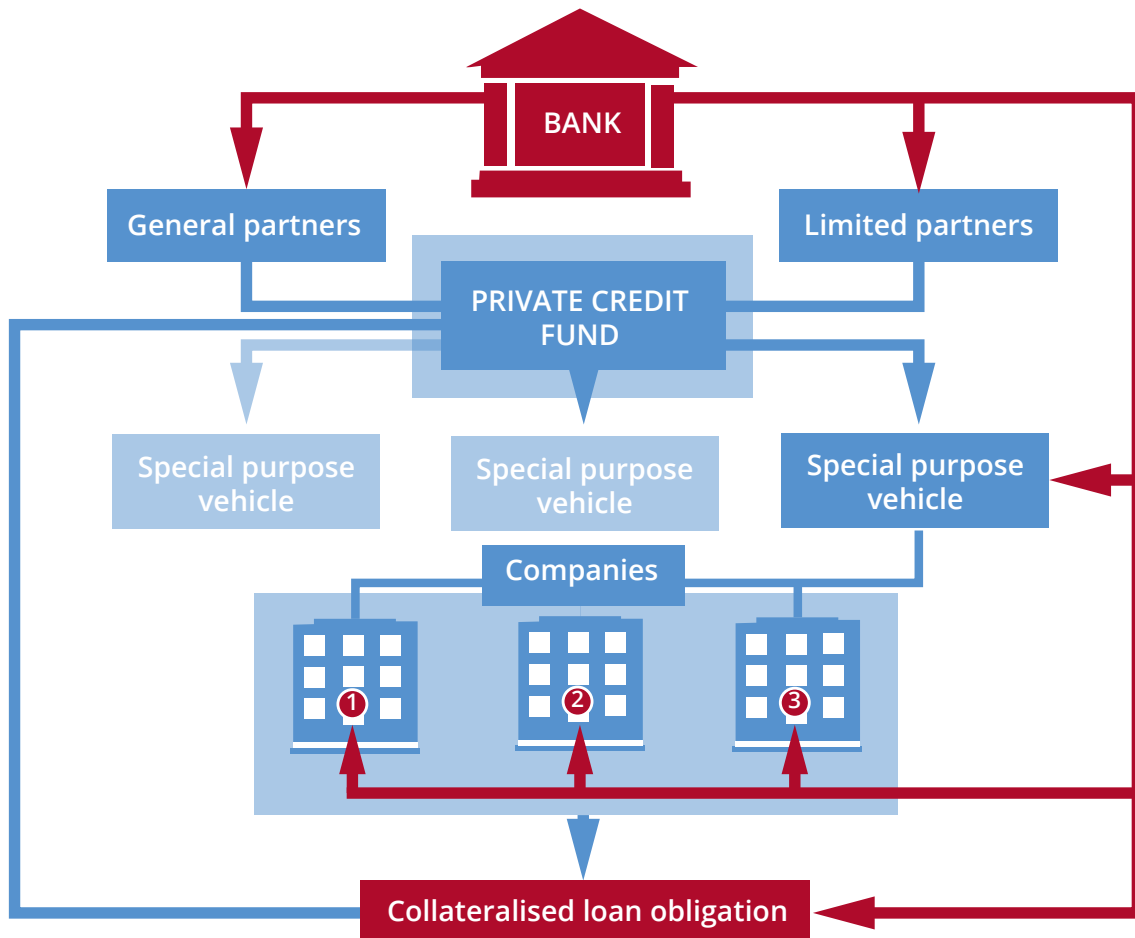
299 Written evidence from the Association for Financial Markets in Europe ([PMG0017](#))

Figure 3: Visualisation of interconnections between banks and private equity funds



Source: Written evidence from Toby Nangle (PMG0039), graphic produced by the Financial Times.

Figure 4: Visualisation of interconnections between private credit and the banking system via a collateralised loan obligation



Source: *Financial Times*, [How banks fuel the private credit boom](#), 1 December 2025.

143. The Financial Policy Committee’s July 2025 report explained that banks directly and indirectly finance private market funds and private equity-backed companies through several channels. Banks “arrange and syndicate loans, offer various forms of [net asset value] based financing, [...] and also typically provide revolving credit facilities to these [private equity]-backed corporates.”³⁰⁰ The Bank of England told us that these loans can become further interconnected with the financial system when securitised via collateralised loan obligations. The Bank warned that: “[collateralised loan obligations] and other parts of the financial system place a degree of reliance on credit ratings. That creates an important role for credit rating agencies in this system of finance. A shock to highly indebted companies could be amplified by these interconnections, with losses and the impact on risk appetite potentially spilling across several markets and sectors.”³⁰¹
144. Nathanaël Benjamin set out a broad overview of these interconnections, which he described as “important, very meaningful, and quite deep.”³⁰² He said:

300 Written evidence from the Bank of England ([PMG0021](#))

301 *Ibid.*

302 [Q 153](#) (Nathanaël Benjamin)

“Banks get involved through different levels of the financing chain for private equity and private credit. They do upstream lending to the investors, to the limited partners, directly. They do midstream lending to the general partners that manage the funds, the private equity or private credit funds, against the total value of a given fund invested in private assets. They do downstream lending directly to the companies, the portfolio companies that receive that funding. In addition, they provide leverage to private credit funds that either compete or partner with them. They also provide financing to limited partners, secured by their own interests in the funds.”³⁰³

145. The Loan Market Association set out what it deems as the three most significant interconnections between UK banks and private credit, in terms of prevalence:

“Co-investment in leveraged loans—Private credit funds cannot generally provide working capital, cash management and other banking services, so banks maintain a vital role in direct lending transactions. Banks and private credit also co-invest in secured leveraged term debt. These relationships have led a number of banks to enter into partnerships with private credit funds, or to establish private credit platforms to compete with them directly.

Fund finance—The growth of private markets has brought with it increased demand from PE and credit funds for liquidity support from the banking sector, in the form of secured subscription lines and NAV facilities.

Synthetic risk transfer (SRT)—Private credit funds have emerged as a key investor in SRT; a structured form of loan securitisation undertaken by banks that provides private credit investors with exposure to a range of assets that may be difficult for funds to access directly.”³⁰⁴

146. We heard that these interconnections are becoming increasingly complex and difficult to monitor. Dr Alireza Abbasi Gorji, Assistant Professor of Business Management, Faculty of Literature and Humanities, University of Birjand, acknowledged the benefits of the “growing interdependence” between banks and private markets for financial innovation, risk diversification and access to diverse pools of capital but warned that it “creates complex channels of contagion” and that such linkages mean that shocks originating in private markets “such as valuation corrections, liquidity crunches, or fund redemption spirals—can quickly spill over into the regulated banking sector.”³⁰⁵ Dr Daniele D’Alvia told us: “Generally, banks’ indirect exposures to non-bank intermediaries have grown in complexity, potentially creating a ‘financial web’ of risk-sharing that is not fully visible to regulators.”³⁰⁶
147. The Bank of England also raised concerns over the visibility of these interconnections. They told us: “the lack of aggregated data on banks’ total concentration exposures to private markets and the various ways in which they are involved makes it difficult to monitor these vulnerabilities.”³⁰⁷

303 Q 153 (Nathanaël Benjamin)

304 Written evidence from the Loan Market Association (PMG0029). Synthetic risk transfers are often used to effect the significant risk transfers referred to in paragraph 53.

305 Written evidence from Dr Alireza Abbasi Gorji (PMG0003)

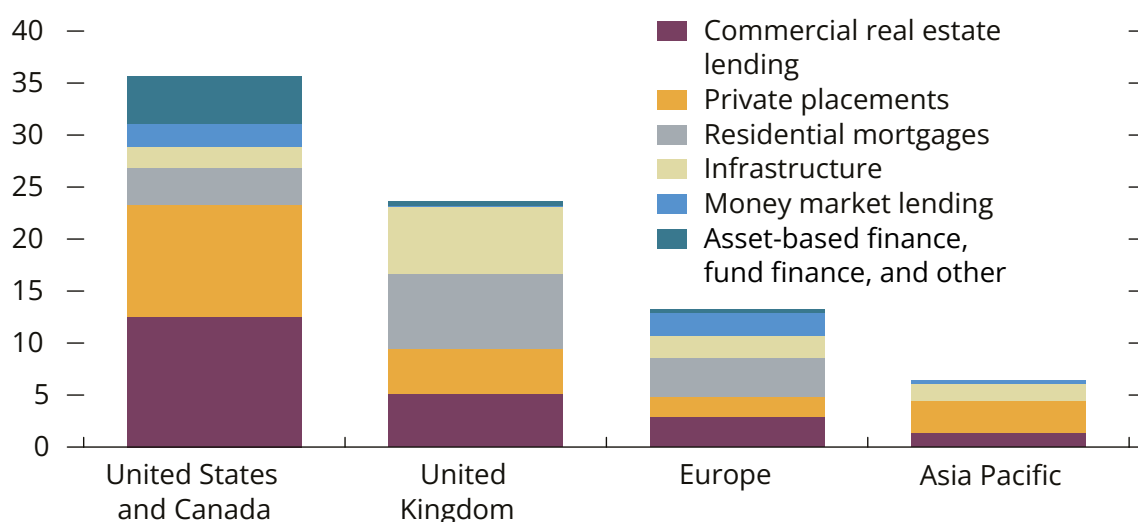
306 Written evidence from Dr Daniele D’Alvia (PMG0008)

307 Written evidence from the Bank of England (PMG0021)

Interconnections between private credit, private equity, and the life insurance sector

148. During this inquiry, the interconnections between the life insurance sector, private credit and private equity were brought to our attention. Whilst we received limited evidence, it appears that some of the risks arising from interconnections between banks and private markets apply equally to the life insurance sector.
149. The interconnections between private markets and the life insurance sector have grown considerably, with analysis by the IMF (Figure 5) showing that approximately 35% of assets held by US life insurers and approximately 23% of those held by UK life insurers were allocated to private credit.³⁰⁸ Toby Nangle, reporter at the Financial Times Alphaville, commented: “The strongest candidate for a risk to financial stability looks to be from the insurance sector.”³⁰⁹

Figure 5: Moody’s survey of insurers’ investment into private credit instruments as a percent of total investment



Source: *The International Monetary Fund, Global Financial Stability Report, October 2025.*

150. As noted in paragraph 19, trends in the US may indicate how the interactions between UK private markets and insurers could develop. Professor Arthur E. Wilmarth Jr. told us that \$1tn of assets, representing 10% of the sector’s total assets under management, are held by insurers which are owned by private capital fund managers.³¹⁰ As noted in paragraph 40, this has been partly driven by the alignment of the investment and lending tenures between the two sectors, making life insurance a natural investor into private markets.
151. As these interconnections appear likely to continue to grow, the implications of these interconnections for the UK’s financial stability merit closer attention. The IMF reported that: “A growing share of insurers’ private credit exposure is sourced through either affiliated private credit managers or partnerships

308 International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025, pp 43–44; Financial Times Alphaville, *If private credit breaks, insurers will fall under the microscope*, November 2025: “Private credit now accounts for more than 35 per cent of total US insurer investments and close to a quarter of UK insurer assets.”

309 Written evidence from Toby Nangle (PMG0039)

310 Written evidence from Professor Arthur Wilmarth Jr (PMG0022)

with private credit managers, which requires special attention because of potential conflicts of interest and the lack of transparency”.³¹¹

152. We asked some of the leading global private credit fund managers whether their firms own captive insurers. We were told that only Apollo directly owns an insurance subsidiary. Tristram Leach told us that of the \$690 billion of credit assets under management, 60% originates from Apollo’s retirement services insurance business³¹², which he emphasised has “never been owned by private equity funds. Athene, our retirement services business, is wholly owned by Apollo. It is essentially our own capital. It is not owned within a private equity fund with differing incentives.”³¹³
153. We were told that Ares and Blackstone do not own captive insurers, though life insurance firms remain large investors in their private credit funds. Daniel Leiter told us that Blackstone does “not own a captive insurance company”, instead it focusses on managing investments on behalf of insurers: “Insurance is a \$250 billion business for us in terms of capital”.³¹⁴ Blair Jacobson told us that Ares utilises the same business model as Blackstone and that Ares does not “have a captive on-balance sheet insurance business”.³¹⁵
154. All three witnesses emphasised the high quality of the assets in which life insurance partners seek to invest. Daniel Leiter told us that Blackstone’s investments on behalf of life insurance partners are into investment grade lending, predominantly infrastructure and asset-based credit.³¹⁶ Tristram Leach explained that, because life insurance firms “collect premium on which they need to pay out generally quite long-dated liabilities, and then they seek to earn safe yield to make a spread between the two”,³¹⁷ as a result “what they need is a very safe yield.”³¹⁸
155. However, echoing concerns raised in paragraph 132, Toby Nangle told us that “there are questions hanging over the ratings”³¹⁹ of private credit assets held by insurers. He pointed to recent reporting by the Financial Times³²⁰ on the IMF’s Global Financial Stability Report October 2025, which showed that a growing proportion of investment classification in the US is conducted by specialist credit rating agencies.³²¹ The accuracy of these ratings has raised concerns regarding misallocation of sub-investment grade products into the ‘investment grade’ bucket.³²²
156. The IMF has highlighted that the classification of products as ‘investment grade’ brings favourable regulatory capital treatment, thereby reducing the amount of capital a life insurer needs to hold against the asset.³²³ Nathanaël Benjamin explained that in “the UK there is also the use of ratings [...] by the insurance industry as part of the matching adjustment”.³²⁴ Misallocation

311 International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025, p 43

312 [Q 132](#) (Tristram Leach)

313 [Q 136](#) (Tristram Leach)

314 [Q 136](#) (Daniel Leiter)

315 [Q 136](#) (Blair Jacobson)

316 [Q 136](#) (Daniel Leiter)

317 [Q 136](#) (Tristram Leach)

318 [Q 135](#) (Tristram Leach)

319 Written evidence from Toby Nangle ([PMG0039](#))

320 Financial Times, *What’s up with private credit ratings?*, October 2025

321 International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025, pp 43–44

322 International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025, p 44

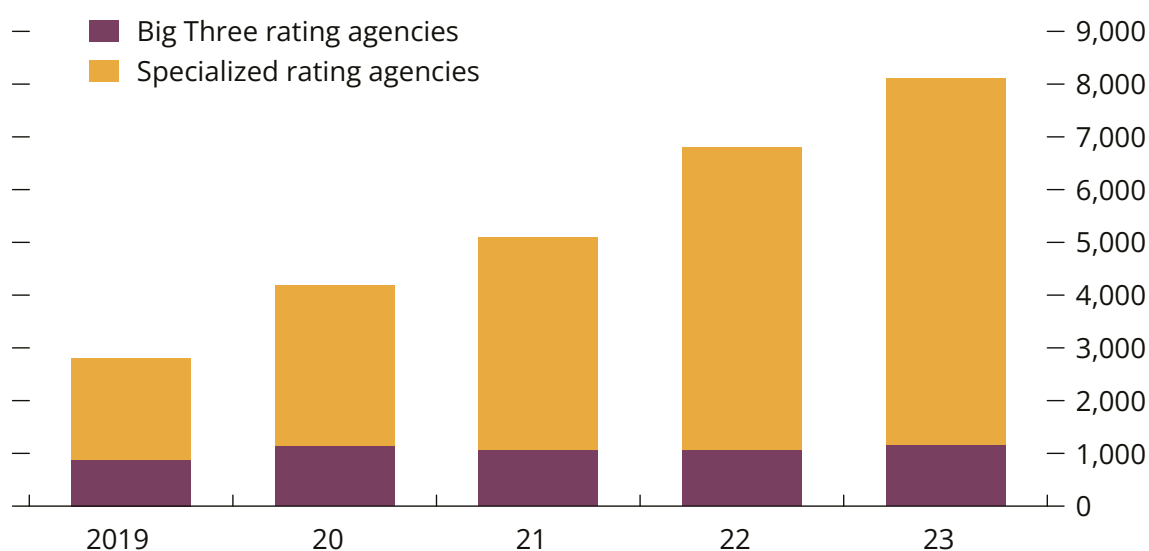
323 International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025, p 44

324 [Q 159](#) (Nathanaël Benjamin)

of credit ratings can leave life insurers holding less capital than they should during an economic shock, a key contributing factor to the Global Financial Crisis. The IMF noted that “it is imperative to keep the risk of inflated ratings minimal by ensuring the soundness of private rating assessments and [requiring] adequate transparency of methodologies and reports.”³²⁵

157. Moreover, we received some concerns regarding the use of differences in regulation between jurisdictions to limit the amount of capital a life insurer must hold. Professor Ludovic Phalippou raised concerns regarding leverage throughout the investment chain, comparable to concerns set out in paragraphs 133–136, as insurers are “allowed to leverage 10 times \$1 invested in a private credit fund”.³²⁶ Toby Nangle echoed these concerns, noting that insurers have proved effective at identifying opportunities for capital efficiency, “either through regulation-shopping the jurisdiction of their funded-reinsurance operations, lending to affiliates, engaging in wholly-owned portfolio securitisation, and seeking private credit ratings.”³²⁷

Figure 6: Privately rated securities held by US insurers (total number)



Source: *The International Monetary Fund, Global Financial Stability Report, October 2025.*

158. Nathanaël Benjamin reassured the Committee that the Bank of England and the PRA are aware of, and actively monitoring, the risks that arise from the interconnections discussed in this section.³²⁸ He shed light on what this investment chain looks like:

“... under this funded reinsurance arrangement, life insurers transfer those annuities to reinsurers overseas—which could be in jurisdictions such as Bermuda or the US, for example—and in turn the assets are being invested or can be invested in private, asset-backed securities”.³²⁹

159. On 17 November, the PRA published the results of its stress tests on the Life Insurance sector, which indicated that the UK’s major life insurance

325 International Monetary Fund, *Global Financial Stability Report, October 2025*, October 2025, p 44

326 [Q 16](#) (Professor Ludovic Phalippou)

327 Written evidence from Toby Nangle ([PMG0039](#))

328 [Q 161](#) (Nathanaël Benjamin)

329 *Ibid.*

companies are resilient to severe but plausible financial market stress scenarios.³³⁰

160. **We did not receive conclusive evidence to determine that private markets either do or do not represent a systemic risk. However, the growth of private credit meets several of the tests of significance for the assessment of systemic risk and therefore is systemically relevant, chiefly through the extent of the sector’s interconnections with systemic parts of the financial system—banking and life insurance. Further work is required to assess and address (if necessary) the broader structural and system-wide vulnerabilities presented by private markets. We welcome the Bank of England’s System Wide Exploratory Scenario to develop this understanding (as detailed below).**
161. **The Bank of England must ensure that it has the appropriate information it needs to fully understand the scale of, and the implications that arise from, the interconnections between the banking system and private credit. The Bank of England must ensure its requests for information are proportionate and avoid duplication, and that it seeks data from the banking system and private credit market as necessary. The Government must ensure that the Bank of England has the appropriate power to collect this information if needed.**
162. **Any response by the Government and the Bank of England to these concerns, including the outcome of the System Wide Exploratory Scenario, must ensure that such action does not inhibit the banking sector’s or private credit’s ability to lend to the real economy.**

Action by the regulators

163. The regulators have already taken action on some of the concerns raised in this Chapter. In 2024, the PRA conducted a thematic review of banks’ private equity related financing activities, focusing on the adequacy of banks’ risk management frameworks. It found that: “many banks are unable to uniquely identify and systematically aggregate or measure their combined credit and counterparty risk exposures to private equity, meaning they cannot monitor comprehensively risks emanating from private markets.”³³¹
164. As noted in paragraph 130, the FCA published the results of a multi-firm review of valuation practices in March 2025. The Financial Policy Committee has welcomed this work.³³² The FCA also highlighted that in June 2025, “we initiated a multi-firm review focusing on conflicts of interest at firms managing private assets. This review will aim to identify and assess areas of potential investor harm and will look to communicate practice to the market to support firms’ management of conflicts.”³³³

330 Prudential Regulation Authority, *Life Insurance Stress Test: 2025 Results*, November 2025: The PRA stress test incorporated a decline in risk-free interest rates, falls in equity and property prices, along with spreads and subsequent defaults and downgrades. The PRA’s stress tests indicated that UK major life insurers’ aggregate Solvency Capital Requirement ratio would decline from 185% to 154%, well above regulatory minimum requirements.

331 Written evidence from the Bank of England ([PMG0021](#))

332 Bank of England Financial Policy Committee, *Financial Policy Committee Record, April 2025*, April 2025, p 4

333 Written evidence from the Financial Conduct Authority ([PMG0040](#))

165. In its session with the Committee in November, the Bank of England announced that it would be conducting a System Wide Exploratory Scenario that will involve the banks, the insurers, private equity companies and pension fund investors. Sarah Breeden told us that it will: “look to apply an economic stress to this complex set of interconnections in order to try to drive through and understand where the losses might arise as part of that.”³³⁴ Participants will engage with the System Wide Exploratory Scenario on a voluntary basis.³³⁵
166. On 4 December 2025, the Bank of England announced its intention to conduct the System Wide Exploratory Scenario, which will conclude in 2026 and will publish its final results in early 2027. The Bank of England announced that this exploratory scenario will include key participants in the private market ecosystem, including traditional and alternative large asset managers, large banks providing credit to both private market funds and private equity-sponsored companies, and institutional investors that are the primary providers of capital to private credit and related public markets.³³⁶
167. **We welcome the Bank of England’s System Wide Exploratory Scenario. We encourage the Bank to complete this exercise as a matter of urgency and to determine whether private credit and private equity in the UK are systemic. We also encourage the Bank to publish timely updates as appropriate; and to share such updates with the Committee.**
168. *The Committee recognises that the Bank of England is conducting its System Wide Exploratory Scenario on a voluntary basis. The Government should keep the powers available to the Bank of England under review, contingent on the outcome of the System Wide Exploratory Scenario.*
169. *As the Bank of England takes forward its work on the System Wide Exploratory Scenario it should consider the following issues highlighted in this report:*
- (a) *The different types of private credit funds and the lending practices of private credit funds focussing on sub-investment grade lending;*
 - (b) *The interconnections between private credit, private equity, and the banking sector (including fund finance, private credit collateralised loan obligations, significant risk transfers, and the secondary trading of private debt);*
 - (c) *The interconnections between private credit and private equity and the insurance sector—particularly the life insurance sector;*
 - (d) *The interconnections between banks and private credit and equity through the securitised lending market, including collateralised loan obligations, significant risk transfers, and liquid credit;*

334 [Q 110](#) (Sarah Breeden)

335 [Q 111](#) (Sarah Breeden)

336 Bank of England, [Bank of England launches system-wide exploratory scenario exercise focused on private markets](#), December 2025

- (e) *The accuracy and reliability of private market valuations; and*
 - (f) *The reliance by private market firms on third party credit ratings agencies, and the accuracy of the ratings provided by said firms.*
170. *Though the FCA’s multi-firm review of private market valuation practices represents a welcome first step, the FCA should monitor the issues it identified and complete its review on conflicts of interest at firms managing private assets as soon as possible. The FCA must share its findings with the Committee.*

The role of the Government

The Government’s responsibility to maintain financial stability

171. The UK’s legislative framework for financial services regulation gives statutory objectives to operationally independent regulators and grants them powers to make rules that advance these objectives. The Bank of England Act 1998 conferred primary responsibility for maintaining the UK’s financial stability to the Bank of England.³³⁷ HM Treasury retains responsibility for maintaining the UK’s financial stability and setting the policy direction in which the regulators operate. HM Treasury can advance financial stability through making recommendations to the Financial Policy Committee on achieving its Financial Stability Objective³³⁸, or legislating to grant new powers to the regulators or to expand their regulatory remit. Additionally, HM Treasury holds the power to make regulations which require the regulators to exercise powers under the Financial Services and Markets Act 2000.³³⁹
172. Additionally, HM Treasury is the backstop to the UK’s financial system during an acute crisis. In response to the Global Financial Crisis, the Government introduced several measures including injecting £137 billion in public money to stabilise the financial system³⁴⁰, and nationalised or took ownership stakes in several banks, including NatWest Group, Northern Rock, and Lloyds Banking Group.³⁴¹ Concerningly, Lord King of Lothbury told us that, due to the high level of national debt, we “are not in a comfortable position. I think we would cope with another crisis, but it would not be easy, and we were in a much stronger position back in 2007–08.”³⁴²
173. Since 2008, HM Treasury has legislated for several reforms to the regulatory framework for financial services which aim to mitigate the impact of financial instability on the wider economy and reduce taxpayers’ exposure. These include capital and liquidity requirements, a bank resolution regime, and the ring-fencing of bank assets. However, these systems remain largely untested.³⁴³
174. As such, it is vitally important that HM Treasury remains engaged and vigilant in monitoring financial stability risks and is prepared to take the steps necessary to mitigate them. Considering this, the Committee was

337 Bank of England Act 1998, [section 2A](#)

338 Bank of England Act 1998, [section 9E](#)

339 Financial Services and Markets Act 2000, [section 3RE](#)

340 House of Commons, [Bank rescues of 2007–09: outcomes and cost](#), October 2018, p 4

341 HM Treasury, [Review of HM Treasury’s response to the financial crisis 2007–09](#), March 2012, pp 20–21

342 [Q 65](#) (Lord King of Lothbury)

343 Banking Act 2009, [section 13](#)

keen to understand the Government’s assessment of the implications of the growth of private markets for financial stability.

The Government’s response to our inquiry

175. HM Treasury recognised that the growth of private markets may pose new risks, to which the Economic Secretary to the Treasury, Lucy Rigby KC MP, repeatedly assured us that the Government was “alive”³⁴⁴. Specifically, the Minister noted that “the growth in private markets comes with new risks, given the sector’s growing complexity and, in some cases, a lack of transparency and the links with the banking system as a whole.”³⁴⁵ When pushed on which risks the Government was most concerned about the Minister clarified that it was private markets’ interconnections with the regulated sector and their lack of transparency;³⁴⁶ Lowri Khan CB CBE, Director for Financial Stability, told us that the department was concerned about the lack of data but did not expand on which data.³⁴⁷
176. We pressed for clarity regarding how HM Treasury is responding to the divergence in international regulatory standards or a potential shock arising from US private credit markets. The Minister told us she is “confident in the regulators’ ability to manage these things because of the mature regulatory framework that we have.”³⁴⁸ HM Treasury did not offer specific details on what measures it would take to mitigate this risk.
177. Given HM Treasury’s recognition of these potential risks, we sought to understand the extent of its independent monitoring of market developments. Lowri Khan told us that the department: has a non-voting member who attends all the Financial Policy Committee meetings; that it supports the Bank of England in international fora such as the Financial Stability Board; and maintains a regular dialogue with the regulators, including the Bank of England.³⁴⁹
178. Evidence from the Government indicated that responsibility for managing these risks sits with the regulators, as the Minister noted: “We [...] very much support the work that is being done by regulators to understand and mitigate those risks.”³⁵⁰ Daniel Rusbridge, Deputy Director for Personal Finances and Funds, suggested that the Treasury’s primary responsibility is “to ensure that our regulators have the necessary tools in order to act, be that retrospectively or, indeed, proactively.”³⁵¹ The Minister also noted that an upcoming remit letter to the Financial Policy Committee would “specifically refer to private markets.”³⁵² The remit letter, published on 26 November 2025, asks the Financial Policy Committee to “prioritise building resilience in NBFIs [Non-bank financial intermediaries] and associated markets, including by working through the Financial Stability Board to improve regulatory frameworks and monitoring across jurisdictions, and using insights gained (e.g. from the System Wide Exploratory Scenario). As

344 [Q 173](#) (Lucy Rigby KC MP)

345 [Q 173](#) (Lucy Rigby KC MP)

346 [Q 191](#) (Lucy Rigby KC MP)

347 [Q 191](#) (Lowri Khan CB CBE)

348 [Q 177](#) (Lucy Rigby KC MP)

349 [Q 181](#) (Lowri Khan CB CBE)

350 [Q 173](#) (Lucy Rigby KC MP)

351 [Q 177](#) (Daniel Rusbridge)

352 [Q 190](#) (Lucy Rigby KC MP)

part of this work, the Committee should continue to consider the risks in private markets.”³⁵³

179. We questioned the Minister as to the actions the Government would take if the Bank of England’s System Wide Exploratory Scenario exercise did conclude that there is systemic risk arising from private markets. The Minister responded that that “would depend on the outcome of such a scenario” and that HM Treasury “would want to respond in a granular and detailed way, based on what comes out of that.”³⁵⁴
180. When pressed on what the Government can do, or is currently doing, to mitigate any risks emerging from the private market sector, we found the department’s responses to be limited to highlighting the action taken by the regulators, with no clear evidence presented in the session of a proactive response to the concerns raised about private markets. Overall, we were concerned that HM Treasury’s response to our concerns lacked detail and demonstrated limited engagement with the issues raised throughout our inquiry.
181. **Our previous report recommended that HM Treasury take greater responsibility for setting the strategic direction to the regulators. During the oral evidence session with the Committee, HM Treasury did not reassure us that it has a firm grasp on the emerging issues related to private markets and their potential impact on financial stability.**
182. **Whilst we recognise that the legislative framework has conferred a financial stability objective on the Bank of England, HM Treasury has a responsibility to maintain the UK’s financial stability, so that the risk that the taxpayer serves as a backstop to the financial system is mitigated. In light of this, we are concerned by what seemed like passivity on the part of HM Treasury.**
183. *The Government is responsible for setting the strategic agenda of financial regulation. Delegation to independent regulators can never equate to an abdication of responsibility. The Government retains this responsibility notwithstanding the delegation of tasks to independent regulators.*
184. *Recognising the importance of this responsibility, we ask that HM Treasury’s response to this report includes: HM Treasury’s plan to support the Bank of England in conducting its System Wide Exploratory Scenario; and details on what the Department is doing proactively to meet its responsibility to maintain financial stability, with respect to assessing and responding to potential risks emerging from the private market sector.*

353 HM Treasury, *Remit and recommendations for the Financial Policy Committee. Letter to Andrew Bailey, Governor of the Bank of England*, November 2025

354 [Q 173](#) (Lucy Rigby KC MP)

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

Growth of private markets

1. The rapid growth of global private credit and equity markets, particularly in the US, presents opportunities and risks for the UK. The Committee welcomes the Bank of England's work to shine a light on these developments; the Government, the Bank of England, the Prudential Regulation Authority, and the Financial Conduct Authority must continue proactively to monitor developments in private markets. (Paragraph 20)
2. Reforms introduced after the Global Financial Crisis—particularly bank capital and liquidity regulatory requirements—have, as intended, encouraged the banking system to retreat from riskier lending, leaving certain segments of the economy, including SMEs, less well served by banks. (Paragraph 34)
3. The rapid growth of private credit and private equity is a response to market demand for assets that provide higher returns from institutional investors during a period of relative lower yields, and greater flexibility for borrowers. Quantitative easing and low interest rates have helped to create these market conditions. (Paragraph 44)
4. Private credit currently remains a small provider of corporate debt in the UK, relative to banks. However, the rapid growth of private credit is likely to continue, and we expect it to become an increasingly significant provider of corporate direct lending. (Paragraph 45)
5. The growth in collateralised loan obligations and significant risk transfers in the UK may pose a potential risk to the UK's financial stability. The Bank of England and the Prudential Regulation Authority should pay close attention to the development of these markets. (Paragraph 56)
6. The UK's corporate debt lending market is increasingly competitive as private credit steps in to fulfil demand that is underserved by banks. Concurrently, banks increasingly lend to, and are in partnership with, private credit funds. As banks have increasingly turned to an 'originate to distribute' model of lending, reflecting the growth of the securitisation market, these interconnections have grown. (Paragraph 67)
7. Throughout the inquiry, we asked for data from the regulators, academics, and industry trade bodies and firms. However, we were not able to obtain extensive or detailed data on the growth of private markets in the UK, the growth of lending provided by private credit, or the scale of interconnections between banks and private markets. We are concerned that this might represent a gap in policy and rule makers' evidence base. (Paragraph 68)
8. *The Bank of England and the Government must ensure they have a comprehensive understanding of lenders to the UK economy, specifically by identifying the proportion of (1) total corporate debt; (2) corporate debt classified by sector, provided by different funding sources, including private credit; and (3) developments in the UK's lending ecosystem as private credit grows.* (Paragraph 69)
9. The differences in the regulation—particularly capital and liquidity regulatory requirements—between the banking system (which creates money) and private credit (which does not) have led to the migration of certain types of lending from banks to private credit funds, as was intended. (Paragraph 76)

SME lending

10. The limited use of debt finance by SMEs to fund growth primarily reflects low appetite to borrow, principally caused by low business confidence in the economy. However, the use of personal guarantees and limited access to support through advice or education have further suppressed demand. (Paragraph 101)
11. Relationship-based lending appears to have declined in the UK, which a growing body of research suggests harms SMEs' ability to access finance when they do wish to borrow. We encourage the Government to consider how to restore access to relationship-based lending as part of its financial services strategy going forward. (Paragraph 102)
12. The regulatory environment has made it more expensive for banks to lend to SMEs, reflecting the higher risks and costs involved in such lending. We are concerned that the commercial attractiveness of lending to SMEs may continue to decline, and that banks may reduce SME lending whilst private credit may not step in. (Paragraph 103)
13. Although smaller and specialist lenders have become increasingly important to the UK SME lending market, regulation continues to constrain their capacity to lend to SMEs. We encourage the Government and the Bank of England to explore what lessons might be learnt from the regulation of community banking sectors in the US and Germany. (Paragraph 113)
14. Whilst the Committee welcomes the Financial Policy Committee's reduction in the appropriate benchmark for the system-wide level for capital requirement, this does not substantively address long-standing concerns with the disproportionate application of the UK's capital and liquidity regulatory regime. Modifying the regulatory constraints on smaller and specialist lenders could help these lenders to grow and they in turn would be better positioned to increase their SME lending. (Paragraph 114)
15. *We welcome the Financial Policy Committee's announcement that it will review several aspects of the capital regime and hope that this can be completed rapidly. The PRA should implement any changes in a way which maximises the amount of bank capital which can be made available to support lending, including to SMEs. The Prudential Regulation Authority should move quickly to implement its proposed changes to the IRB approval process and risk weightings of assets.* (Paragraph 115)

Financial stability

16. We did not receive conclusive evidence to determine that private markets either do or do not represent a systemic risk. However, the growth of private credit meets several of the tests of significance for the assessment of systemic risk and therefore is systemically relevant, chiefly through the extent of the sector's interconnections with systemic parts of the financial system—banking and life insurance. Further work is required to assess and address (if necessary) the broader structural and system-wide vulnerabilities presented by private markets. We welcome the Bank of England's System Wide Exploratory Scenario to develop this understanding (as detailed below). (Paragraph 160)
17. The Bank of England must ensure that it has the appropriate information it needs to fully understand the scale of, and the implications that arise from, the interconnections between the banking system and private credit. The

Bank of England must ensure its requests for information are proportionate and avoid duplication, and that it seeks data from the banking system and private credit market as necessary. The Government must ensure that the Bank of England has the appropriate power to collect this information if needed. (Paragraph 161)

18. Any response by the Government and the Bank of England to these concerns, including the outcome of the System Wide Exploratory Scenario, must ensure that such action does not inhibit the banking sector's or private credit's ability to lend to the real economy. (Paragraph 162)
19. We welcome the Bank of England's System Wide Exploratory Scenario. We encourage the Bank to complete this exercise as a matter of urgency and to determine whether private credit and private equity in the UK are systemic. We also encourage the Bank to publish timely updates as appropriate; and to share such updates with the Committee. (Paragraph 167)
20. *The Committee recognises that the Bank of England is conducting its System Wide Exploratory Scenario on a voluntary basis. The Government should keep the powers available to the Bank of England under review, contingent on the outcome of the System Wide Exploratory Scenario.* (Paragraph 168)
21. *As the Bank of England takes forward its work on the System Wide Exploratory Scenario it should consider the following issues highlighted in this report:*
 - (a) *The different types of private credit funds and the lending practices of private credit funds focussing on sub-investment grade lending;*
 - (b) *The interconnections between private credit, private equity, and the banking sector (including fund finance, private credit collateralised loan obligations, significant risk transfers, and the secondary trading of private debt);*
 - (c) *The interconnections between private credit and private equity and the insurance sector—particularly the life insurance sector;*
 - (d) *The interconnections between banks and private credit and equity through the securitised lending market, including collateralised loan obligations, significant risk transfers, and liquid credit;*
 - (e) *The accuracy and reliability of private market valuations; and*
 - (f) *The reliance by private market firms on third party credit ratings agencies, and the accuracy of the ratings provided by said firms.* (Paragraph 169)
22. Though the FCA's multi-firm review of private market valuation practices represents a welcome first step, the FCA should monitor the issues it identified and complete its review on conflicts of interest at firms managing private assets as soon as possible. The FCA must share its findings with the Committee. (Paragraph 170)
23. Our previous report recommended that HM Treasury take greater responsibility for setting the strategic direction to the regulators. During the oral evidence session with the Committee, HM Treasury did not reassure us that it has a firm grasp on the emerging issues related to private markets and their potential impact on financial stability. (Paragraph 181)

24. Whilst we recognise that the legislative framework has conferred a financial stability objective on the Bank of England, HM Treasury has a responsibility to maintain the UK's financial stability, so that the risk that the taxpayer serves as a backstop to the financial system is mitigated. In light of this, we are concerned by what seemed like passivity on the part of HM Treasury. (Paragraph 182)
25. *The Government is responsible for setting the strategic agenda of financial regulation. Delegation to independent regulators can never equate to an abdication of responsibility. The Government retains this responsibility notwithstanding the delegation of tasks to independent regulators.* (Paragraph 183)
26. *Recognising the importance of this responsibility, we ask that HM Treasury's response to this report includes: HM Treasury's plan to support the Bank of England in conducting its System Wide Exploratory Scenario; and details on what the Department is doing proactively to meet its responsibility to maintain financial stability, with respect to assessing and responding to potential risks emerging from the private market sector.* (Paragraph 184)

APPENDIX 1: LIST OF MEMBERS AND DECLARATIONS OF INTEREST

Members

Baroness Bowles of Berkhamsted
 Baroness Donaghy
 Lord Eatwell
 Lord Forsyth of Drumlean (Chairman)
 Lord Grabiner
 Lord Hill of Oareford
 Lord Hollick
 Lord Kestenbaum
 Lord Lilley
 Baroness Noakes
 Lord Sharkey
 Lord Smith of Kelvin
 Lord Vaux of Harrowden

Declarations of interest

Baroness Bowles of Berkhamsted
Non-Executive Director, London Stock Exchange PLC, regulated investment exchange supervised by the FCA
Shareholder and Non-Executive Director, Valloop Holdings Limited
Non-Executive Director, Valloop Impact Captive
Investor in collective investment undertakings

Baroness Donaghy
No relevant interests declared

Lord Eatwell
Advisor, Palamon Capital Partners LLP (a private equity company)
Non-Executive Director, Unity Trust Bank
Investments via collective investment funds

Lord Forsyth of Drumlean (Chairman)
No relevant interests declared

Lord Grabiner
Investments in financial services entities disclosed in the Register of Interests

Lord Hill of Oareford
Advisor, Santander SA
Advisor, Freshfields
General business and strategic advice to Greenbrook (financial communications consultancy)

Lord Hollick
Shareholder, KKR (private equity and credit fund manager)
Shareholder, G.P. Bullhound (tech fund manager)
Shareholder, Salica Investments (tech and credit fund manager)

Lord Kestenbaum
Director of several investment entities associated with the Rothschild Group
Director, JPMorgan Japanese Investment Trust PLC (investment company)

Lord Lilley
No relevant interests declared

Baroness Noakes
Investments in financial services entities disclosed in the Register of Interests

Lord Sharkey

No relevant interests declared

Lord Smith of Kelvin

No relevant interests declared

Lord Vaux of Harrowden

No relevant interests declared

A full list of members' interests can be found in the Register of Lords' Interests:
<https://www.parliament.uk/hregister>

Specialist Advisors

Professor Rosa Lastra

Specialist expert advisor to the Banco de España in its inquiry into the independence, accountability, and transparency of the Banco de España

Member of the Monetary expert panel that advises the European Parliament (ECON)

Expert witness in an international banking arbitration case involving the Republic of Poland

Specialist adviser to the Bank of England on Digital Assets (occasional; non-remunerated)

Michael Raffan

Partner, Freshfields LLP

Member of HM Treasury's Banking Liaison Panel

Member of TheCityUK's Long-Term Competitiveness Group

Member of TheCityUK's US Market Advisory Group Technical Working Group

Member of the Advisory Board, Financial Services Lawyers Association

Investments in various collective investment vehicles

APPENDIX 2: LIST OF EVIDENCE AND COMMITTEE ACTIVITY

Evidence is published online at <https://committees.parliament.uk/work/9235/growth-of-private-markets-in-the-uk-following-reforms-introduced-after-2008/publications/>.

Evidence received by the committee is listed below in alphabetical order.

Alphabetical list of witnesses

| | | |
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| Professor Kern Alexander, Chair for International Financial Law and Regulation, University of Zurich, and Director of Studies in Law and Finance, Queens' College, University of Cambridge | PMG0028 PMG0032 | QQ 1–15 |
| The Alternative Credit Council | PMG0014 | |
| Ignazio Angeloni, Fellow, Institute for European Policymaking, Bocconi University, and Senior Policy Fellow, SAFE, Goethe University | PMG0023 | |
| Apollo Global Management | PMG0046 | QQ 131–140 , Tristram Leach, Partner and Co-Head of European Credit |
| Ares Management Corporation | | QQ 131–140 , Blair Jacobson, Partner and Co-President |
| The Association of British Insurers (ABI) | PMG0019 PMG0047 | |
| The Association for Financial Markets in Europe (AFME) | PMG0017 | |
| Aviva | PMG0044 | |
| Sheila Bair, Former Chair, Federal Deposit Insurance Corporation (FDIC) | PMG0026 | |
| Bank of England | PMG0021 PMG0043 | QQ 107–122 , Andrew Bailey, Governor; and Sarah Breeden, Deputy Governor for Financial Stability QQ 152–161 , Nathanaël Benjamin, Executive Director for Financial Stability Strategy and Risk |

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| Barclays | | QQ 162–172 , Stephen Dainton, President of Barclays Bank plc and Head of Investment Bank Management |
| Dr Vincenzo Bavoso, Professor of Commercial Law, University of Manchester | PMG0004 | |
| Blackstone | | QQ 131–140 , Daniel Leiter, Senior Managing Director, Head of International and Global Head of Liquid Credit Strategies, Blackstone Credit and Insurance |
| Professor David Blake, Professor of Finance, Bayes Business School, City St George's, University of London | PMG0002 | |
| British Business Bank | PMG0025 | QQ 48–62 , Louis Taylor CBE, Chief Executive Officer |
| British Emerging Manager Institute | PMG0001 | |
| British Private Equity & Venture Capital Association (BVCA) | PMG0016 | QQ 123–130 , The Rt Hon Michael Moore, Chief Executive Officer |
| Professor Patrick Corrigan, Professor of Law, Notre Dame Law School | PMG0030 | |
| Dr Daniele D'Alvia, Lecturer in Banking and Finance Law and Associate Researcher at the European Banking Institute, Queen Mary University of London | PMG0008 | |
| Sir Howard Davies, Former Chair, NatWest Group, and Former Chair, Financial Services Authority (FSA) | PMG0020 | QQ 14–151 |
| Deloitte | PMG0033 | |
| European Leveraged Finance Association | PMG0011 | |
| Professor Eilís Ferran FBA, Professor of Company and Securities Law, University of Cambridge | PMG0024 | |

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|---|-------------------------|---|
| Professor Charles Goodhart CBE FBA, Emeritus Professor of Banking and Finance, Financial Markets Group, London School of Economics and Political Science (LSE) | PMG0034 | |
| Martin McTague OBE, National Chair, Federation of Small Businesses (FSB) | | QQ 48–62 |
| Financial Conduct Authority (FCA) | PMG0040 | |
| Professor Tim Congdon CBE FREcon, Chair, Institute of International Monetary Research, University of Buckingham | PMG0038 | |
| Apostolos Gkoutzinis, Partner in Corporate Finance, Securities and Leveraged Finance, Milbank LLP | | QQ 74–81 |
| Professor Simon Gleeson, Visiting Professor, Faculty of Law, University of Oxford, and Consultant, Clifford Chance | | QQ 1–15 |
| Dr Alireza Abbasi Gorji, Assistant Professor, Faculty of Literature and Humanities, University of Birjand, Birjand, Iran | PMG0003 | |
| Handelsbanken plc | PMG0035 | |
| HM Treasury | | QQ 173–191 , Lucy Rigby KC MP, Economic Secretary to the Treasury and City Minister; Lowri Khan CB CBE, Director of Financial Stability; and Daniel Rusbridge, Deputy Director for Personal Finances and Funds |
| HSBC | | QQ 162–172 , Michael Roberts, Chief Executive Officer of HSBC Bank plc and Chief Executive Officer of Corporate and Institutional Banking |
| The Investment Association | PMG0013 | |
| Professor Arthur E. Wilmarth, Jr., Professor Emeritus of Law, George Washington University Law School | PMG0022 | QQ 39–47 |

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|---|-------------------------|--|
| Dr Narine Lalafaryan, Assistant Professor of Corporate Law, Faculty of Law, University of Cambridge, and Fellow, Cambridge Endowment for Research in Finance | PMG0007 | QQ 16–29 |
| Professor Marco Lamandini, Professor of Commercial Law, University of Bologna, and Professor David Ramos Muñoz, Associate Professor of Commercial Law, Universidad Carlos III de Madrid | PMG0045 | |
| Legal and General | PMG0037 | QQ 141–151 , Charlie Nunn, Group Chief Executive |
| Lloyds Banking Group | PMG0029 | |
| Loan Market Association (LMA) | PMG0029 | |
| M&G plc | | QQ 123–130 , Joseph Pinto, Chief Executive Officer of Asset Management |
| Professor Frédéric Malherbe, Professor of Economics and Finance, University College London, and Chiara Lattanzio, PhD student in Financial Economics, University College London | PMG0031 | |
| Managed Funds Association (MFA) | PMG0012 | |
| MSCI Limited | PMG0010 | |
| Toby Nangle, Reporter, FT Alphaville | PMG0039 | |
| OakNorth Bank | PMG0027 | QQ 82–94 , Mark Steele, Chief Risk Officer |
| Paragon Banking Group | PMG0041 | QQ 82–94 , Nigel Terrington, Chief Executive Officer |
| Preqin Ltd | PMG0048 | |
| Professor Ludovic Phalippou, Professor of Financial Economics, Saïd Business School, University of Oxford | | QQ 16–29 |
| Positive Money | PMG0015 | |

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| Professor Raghavendra Rau, Sir Evelyn de Rothschild Professor of Finance, Cambridge Judge Business School, University of Cambridge | <u>PMG0036</u> | |
| Richard Ridyard, Senior Lecturer in Law, Liverpool John Moores University | <u>PMG0018</u> | |
| ScaleUp Institute | | <u>QQ 48–62</u> , Irene Graham OBE, Chief Executive Officer |
| TheCityUK | <u>PMG0009</u> | |
| UK Finance | <u>PMG0042</u> | <u>QQ 95–106</u> , David Postings, Chief Executive Officer |
| Nicolas Véron, Senior Fellow, Bruegel, and Senior Fellow, Peterson Institute for International Economics (PIIE) | | <u>QQ 30–38</u> |

APPENDIX 3: CALL FOR EVIDENCE

Inquiry into the growth of private markets in the UK following reforms introduced after 2008

The Financial Services Regulation Committee, chaired by Lord Forsyth of Drumlean, has launched an inquiry into the growth of private markets³⁵⁵ in the UK following reforms introduced after 2008, in particular:

- Whether the regulatory capital and liquidity reforms introduced after 2008 have reduced banks' ability or willingness to lend, pushing risk away from the banking sector and towards private markets.
- How much visibility the Bank of England has on the size of these private markets, their interconnections with the banking sector, and any potential spillover risks.

When responding, the Committee requests that, where possible, respondents provide verifiable data to inform their answers. The Committee is seeking evidence on the following questions:

- (1) Has bank lending to the real economy in the UK reduced as a proportion of the total volume of finance provided annually since 2008? If so, to what extent can this change be attributed to the reforms to the UK's regulation of bank capital and liquidity requirements? To what extent has any reduction led to an increase in finance by private markets?
- (2) What interconnections exist between the UK's banking sector and private markets? How have these interconnections changed since 2008, and how do you expect them to continue to develop?
- (3) What are the implications of the growth in private markets, and interconnections with the wider financial services sector, for lending to the real economy and the UK's financial stability?
- (4) How transparent are the valuations, price discovery mechanisms, and structure of ownership of assets adopted by private markets? Does the Bank of England have sufficient visibility in non-bank finance, and what changes, if any, should be made to address this?
- (5) Are there systemic risks that the Bank of England should be aware of regarding non-bank financial intermediation? If so, how can these risks be mitigated?
- (6) How has demand for finance from businesses changed since 2008, and how do you expect this will develop?
- (7) How has the regulation of bank capital and liquidity requirements affected the ability and willingness of banks to provide lending to the real economy? Are there disincentives in regulation that inhibit businesses' ability and willingness to access finance through banks?

³⁵⁵ Private markets are part of the non-bank sector. The term non-bank financial intermediation (NBFIs) is used by the UK's regulators (the FCA, Bank of England/PRA) and internationally, such as by the Financial Stability Board (FSB) to describe a diverse set of financial activities, entities, and infrastructure, provided by non-bank institutions. See: Financial Stability Board, *Non-Bank Financial Intermediation*, last updated December 2025

- (8) To what extent do private markets have a competitive advantage over the banking sector to provide finance to businesses; if so, why? To what extent are any competitive advantages regulatory in nature?
- (9) What, if any, reforms to bank capital regulation could be implemented to increase the risk appetite of the banking sector to provide lending to the real economy?
- (10) What can the UK learn from other jurisdictions, in particular the US and the EU?

Closing date: 11.59pm on Thursday 18 September 2025