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Proposed Topic for Inquiry

Rebalancing Risk and Credit Allocation: The Role of Private Markets in Post-2008 UK Financial Sector Reforms

This submission examines the structural shift in the United Kingdom's financial landscape following the regulatory reforms introduced after the 2008 global financial crisis, with a focus on the implications for business management and finance. Specifically, it analyses whether post-crisis capital and liquidity requirements have contributed to a decline in traditional bank lending, thereby accelerating the growth of private markets as alternative finance providers.

From a business management perspective, the inquiry is highly relevant due to its influence on firms' access to capital, cost of borrowing, and financial strategy formulation. The growing prominence of non-bank financial intermediation (NBFI)—including private equity, venture capital, and direct lending—has reshaped how businesses secure funding, manage financial risks, and pursue growth. This shift may indicate a reallocation of risk from regulated banking institutions to less transparent private markets, raising questions about oversight, valuation integrity, and systemic vulnerabilities.

The abstract outlines the key concerns of the inquiry: the extent of reduced bank lending, evolving interconnections between banks and private markets, and the implications for financial stability and economic productivity. It also highlights the challenge regulators face in maintaining visibility over NBFI activities and the need to reassess whether current regulatory frameworks strike the right balance between stability and competitiveness. The UK's experience is contextualised within broader international developments, including comparisons with the US and EU financial ecosystems.

The findings of this inquiry will hold critical insights for corporate finance managers, institutional investors, and policymakers seeking to understand the changing dynamics of capital provision and risk distribution in the UK economy. This research ultimately contributes to the discourse on how regulatory design can support both financial stability and sustainable business growth.

Submission Context

This written evidence is submitted in response to the House of Lords Financial Services Regulation Committee's inquiry into the **growth of private markets in the UK following reforms introduced after 2008**. The submission is prepared by Dr Alireza Abbasi Gorji, a researcher and academic in Business Management, with expertise in financial systems, risk modelling, and regulatory economics. The insights offered draw upon academic research, international regulatory comparisons, and empirical evidence concerning the shifting dynamics of credit intermediation in the UK economy.

This submission aims to critically examine:

- The impact of post-crisis regulatory capital and liquidity reforms on traditional bank lending;
- The corresponding expansion of private markets and the systemic implications thereof;
- The evolving interconnections between banks and private capital providers;
- Regulatory visibility, transparency, and resilience considerations; and
- Practical policy recommendations to foster a more balanced and stable financial ecosystem.

The analysis is particularly relevant to stakeholders in financial policy, bank regulation, and institutional investment, and is intended to support evidence-based decision-making by the Committee. Where appropriate, references to international frameworks and comparative models from the US and EU are included to provide broader context and potential policy benchmarks.

1. Post-Crisis Bank Regulation and the Decline of Traditional Lending

Following the 2008 financial crisis, UK regulators implemented rigorous capital and liquidity reforms under Basel III and national frameworks to strengthen financial stability. While these regulations successfully reduced systemic banking risk, they have also imposed tighter lending standards and elevated capital buffers for banks. This has constrained the ability and willingness of banks to provide credit to businesses, particularly small and medium-sized enterprises (SMEs) and high-risk sectors.

Empirical studies and Bank of England data suggest that bank lending to the real economy, as a proportion of total finance, has gradually declined over the past 15 years. The increased cost of capital compliance, coupled with internal risk-weighted asset (RWA) models, has made banks more selective, often favouring lower-risk, asset-backed lending. Consequently, firms with innovative or growth-oriented business models have increasingly turned to private capital providers who offer more flexible and tailored financing terms.

This phenomenon reflects a regulatory trade-off between risk aversion and credit accessibility. While prudential reforms were necessary, they have unintentionally redirected risk-taking behaviour from banks to private markets, which operate outside the tight regulatory perimeter. This shift warrants a recalibration of policy frameworks to ensure the stability of both sectors.

2. Rise of Private Markets and Financial Intermediation Beyond Banks

Private markets—comprising private equity, venture capital, infrastructure funds, and direct lending—have grown significantly in the UK over the last decade. According to FSB and OECD reports, non-bank financial intermediation (NBFI) now constitutes over 40% of global financial assets, and the UK is no exception to this trend.

The appeal of private markets lies in their ability to provide bespoke, long-term, and patient capital that banks are increasingly reluctant to offer. Private capital also tends to be more agile, with leaner decision-making structures and greater risk tolerance, particularly in the early-stage innovation and infrastructure sectors. This has filled critical funding gaps in areas like green transition, digital infrastructure, and high-tech start-ups.

However, these markets present regulatory blind spots. Private valuations often lack mark-to-market transparency; disclosure requirements are limited; and pricing mechanisms vary widely. As a result, the Bank of England and other regulators face challenges in monitoring market size, risk exposures, and leverage levels. The lack of visibility increases the risk of contagion, especially if macroeconomic shocks or liquidity mismatches arise.

Strengthening data-sharing frameworks and embedding scenario-based stress testing across NBFIs could help illuminate potential vulnerabilities and enable more proactive oversight.

3. Interconnections, Systemic Risks, and Financial Stability Implications

The growing interdependence between traditional banks and private markets is a double-edged sword. On one hand, it fosters financial innovation, risk diversification, and access to diverse pools of capital. On the other, it creates complex channels of contagion. For instance, banks frequently provide credit facilities or fund investments through special purpose vehicles (SPVs) that support private market transactions. They also invest directly in private market funds or act as intermediaries for high-net-worth clients.

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. This was evident during the COVID-19 pandemic, when several real estate and credit funds-imposed redemption freezes due to liquidity constraints.

Despite this, regulatory oversight remains fragmented. Unlike banks, most private capital entities are not subject to consolidated supervision, capital adequacy requirements, or systemic risk buffers. Furthermore, leverage within these entities is often opaque and may be procyclical. Therefore, the UK must prioritise macroprudential surveillance tools that capture cross-sector exposures, maturity mismatches, and shadow banking activities.

Aligning stress-testing regimes and enhancing coordination between the Bank of England, FCA, and international regulatory bodies is essential for safeguarding financial resilience.

4. Business Demand, Competitive Advantage, and the Way Forward

The evolution of business finance demand since 2008 has been shaped by digitisation, globalisation, and post-pandemic recovery needs. Many firms now prefer funding options that provide speed, flexibility, and less stringent collateral requirements—advantages typically offered by private markets over traditional banks.

Private markets benefit from competitive edges such as regulatory light-touch, innovation in structuring deals, and greater appetite for risk. This advantage is particularly regulatory in nature; while banks face rigorous stress tests, disclosure mandates, and capital adequacy requirements, private market actors operate in a less encumbered space.

This asymmetric playing field not only distorts competition but may inadvertently funnel capital away from the banking system, undermining its central role in financial intermediation. To rebalance, the UK must explore pragmatic regulatory reforms that incentivise bank lending without compromising stability.

Potential solutions include recalibrating the capital treatment of SME loans, revisiting internal risk models, and developing public-private co-lending mechanisms. Furthermore, greater alignment with US and EU innovations—such as the US Business Development Companies (BDCs) or the European Investment Fund—could help the UK enhance SME financing through hybrid funding structures.

We Recommend

- Introducing risk-weighted capital relief for banks that lend to productivity-enhancing sectors (e.g., SMEs, green infrastructure).
- Establishing a real-time data-sharing protocol between the Bank of England and major private market actors.
- Creating a joint supervisory framework for monitoring bank–NBFI interlinkages and systemic spillovers.
- Piloting sandbox regimes to test innovative, compliant financing models bridging private and bank capital.
- Promoting UK-based securitisation of private market assets to improve transparency and liquidity.
- Benchmarking against EU and US blended finance schemes to enhance public-private capital mobilisation.

Conclusion

The post-2008 financial regulatory reforms in the United Kingdom were instrumental in enhancing the resilience of the banking sector. However, they also had the unintended consequence of reducing banks' capacity and risk appetite for lending, particularly to SMEs and high-growth sectors. This has contributed to the rapid expansion of private markets, which have stepped in to meet the growing demand for flexible, tailored finance.

While private markets have enriched the UK's financial ecosystem, their ascent introduces new challenges. These include limited transparency in asset valuation and ownership structures, potential liquidity mismatches, and inadequate regulatory oversight. The increasing interconnections between banks and private markets—via credit facilities, investment structures, and client advisory services—mean that risks can no longer be neatly siloed. A disruption in one corner of the financial system could propagate across institutions and markets, with potentially systemic consequences.

The Bank of England and other regulatory bodies must now address two parallel imperatives: supporting the dynamism and innovation that private markets bring, while ensuring that these markets do not become sources of opaque and unmanaged financial risk. Enhancing visibility, improving risk surveillance, and encouraging greater data transparency in non-bank financial intermediation are key priorities.

Furthermore, regulatory asymmetry between banks and private markets requires urgent attention. A recalibration of capital requirements, alongside incentives for responsible lending and co-investment, could re-empower the banking sector to play a more proactive role in supporting the real economy.

Ultimately, the UK should aim for a harmonised, proportionate, and forward-looking regulatory approach that preserves financial stability, fosters competition, and ensures inclusive access to finance. By learning from international examples and encouraging constructive engagement between regulators, banks, and private capital providers, the UK can build a more balanced and resilient financial system fit for the evolving demands of the economy.

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