



Financial Services Regulation Committee

Corrected oral evidence: The growth of private markets in the UK following reforms introduced after 2008

Tuesday 11 November 2025

9.05 am

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Members present: Lord Forsyth of Drumlean (The Chair); Baroness Donaghy; Lord Eatwell; Lord Grabiner; Lord Hollick; Lord Kestenbaum; Baroness Noakes; Lord Sharkey; Lord Vaux of Harrowden.

Evidence Session No. 15

Heard in Public

Questions 162 – 172

Witnesses

I: Stephen Dainton, President of Barclays Bank plc and Head of Investment Bank Management; Michael Roberts, Chief Executive Officer of HSBC Bank plc and Chief Executive Officer of Corporate and Institutional Banking.

USE OF THE TRANSCRIPT

1. This is a corrected transcript of evidence taken in public and webcast on www.parliamentlive.tv.

Examination of witnesses

Witnesses: Stephen Dainton and Michael Roberts.

Q162 The Chair: Welcome to today's meeting, which is the 15th oral evidence session as part of the committee's inquiry into the growth of private markets in the UK following the reforms introduced after 2008. Thank you, Mr Dainton, for attending, and thank you, Mr Roberts, for agreeing to appear online from Hong Kong. The session is open to the public, broadcast live and subsequently accessible via the Parliamentary website. A verbatim transcript will be taken of the evidence and will be put on the parliamentary website. A few days after this session you will be sent a copy to check it for accuracy, and it would be helpful if you could advise us of any corrections as quickly as possible. If, after this session, you want to clarify or amplify any points made during your evidence, or have any additional points to make, you are welcome to submit supplementary written evidence to us.

Would you just like to make a short opening statement? We shall start with you, Mr Dainton.

Stephen Dainton: Thank you for the opportunity to speak to you all this morning. I am the president of Barclays Bank plc, and head of the investment bank management team. I joined Barclays Bank eight years ago in the capacity of one of the co-heads of markets.

There is no doubt that private markets have grown substantially, certainly post GFC and materially, in the course of the past 10 years. The asset class—that is private equity, private credit and infrastructure—is obviously due to be greater than \$15 trillion of AUM; it is a material asset class in all its shapes.

Barclays is a large, wholesale and consumer bank; we have 85,000 employees and compete globally in all our operating businesses. The role of private markets here in the UK is critical and, having listened to some other testimony to this committee, I would entirely agree that the ecosystem has evolved dramatically in the past 10 years. Operating in that ecosystem, we intend not only to help private credit and private equity grow, but crucially to help growth. We believe that each part of the ecosystem provides substantial opportunities for financing for early-stage scale-up and grow-up companies, which is really important here in the UK.

Ahead of the Scottish Global Investment Summit, I wrote an op-ed piece where I expressed very strongly that growth is evident here in the UK, facilitated by capital formation at every single level. That is very important to recognise. From that perspective, we have the support of the Bank of England. A number of the things that the governor and deputy governor have done—earlier than most of the other regulators that we deal with—is to look at the observation of the impact of that lending into the private world, that is private equity and private credit, and ensure that there is a pathway of observation in a more opaque

environment than perhaps regulators have been used to operating in. I give the deputy governor and the governor huge plaudits for bringing that to bear for the industry as a whole.

The Chair: I will ask Mr Roberts to speak in a moment but, just on that point, you say it was a good thing that a pathway that was opaque has been shone on. Do you think that there is reason to be concerned when that light is shone on it?

Stephen Dainton: No, the opportunity is early to ensure that the current opaqueness is just having a light shone on it. It does not mean that I am concerned about the fact that the asset class is relatively opaque, but it does mean that you have, and will have—certainly from here with the Bank of England—a greater level of transparency, and you will see other regulators follow. So I applaud their leadership in that.

The Chair: Mr Roberts?

Michael Roberts: Yes, thank you Lord Chair for the invitation; we are very pleased to support the important work of this committee. I am the CEO of HSBC Bank plc, and the CEO of our corporate and institutional banking globally. Just a bit of background on me: I have been in banking for almost 40 years, about half of which was in the US and half was abroad. I have had my current role for about the last year, and previous to that I was the head of our Americas division, based in New York. As you know, HSBC is a global bank. We are headquartered in the UK with assets over \$3 trillion. We are extremely committed to the UK, including through our ring-fence bank, HSBC Bank UK, based in Birmingham. However, we also operate in 57 countries around the world and are really highly focused on our global footprint to allow us to connect to our clients with diverse opportunities globally.

To set the scene for today's session, I would like to make three points from our perspective. First, it is important to note that private markets are an established part of the ecosystem. I understand your focus is primarily on private credit: this is relatively small but growing very quickly. Private market firms play a useful role in providing capital to the real economy in certain sectors, in our opinion, and we see them as complementary to the more traditional functions and types of lending that banks provide. For example, insurers and pension funds have traditionally been and continue to be crucial buyers of infrastructure finance, an activity that we are very involved in. That is important because their involvement allows us to release capital to reinvest in other projects. With the increase in private credit, where private firms are lending directly to corporates, we are seeing additional financing capacity come online at a price point that we cannot necessarily provide given our very high capital requirements, which are around 15.5% today.

Ultimately, the availability of a diverse range of financing options is important as it boosts system-wide origination capacity, not only for banks but for the entire system, which will be critical, given the scale of infrastructure required over the coming decades. Banks are therefore

naturally involved at all stages, and we remain important counterparties for the private credit clients. We are not the biggest player, and while we are involved in the space, we have taken a very conservative approach.

When thinking about the interconnectedness, which I know is an important topic, it is important to note that there is a fundamental difference between banks like us lending directly to our clients and when we lend to private credit funds. For direct lending by banks, losses are absorbed directly by bank capital, so shielding depositors. In private credit, any losses fall straight to the underlying investors—the LPs—which may be pension funds or similar types of investors that are effectively providing the capital directly. This means that, in comparison to the immediate exposure to losses in direct lending when banks lend to private credit funds, we are normally taking secured and/or senior positions, so we have considerable insulation from losses.

Secondly, it is also right to look at why these trends have emerged. As noted, the UK has taken a conservative approach to bank regulation at every level. Capital requirements are the highest globally when combined with ring-fencing and are notably higher than what the FPC originally concluded as optimal in 2015. This has constrained our ability and the banking system's ability to compete and support customers directly and has led to a necessary evolution of business models.

The work being done by the Government, including through their financial services growth and competitive strategy in the Leeds Reforms, is a step in the right direction. But more needs to be done to ensure that the wider capital and regulatory framework enables banks to play a full role in supporting the UK economy and the Government's growth agenda.

Finally, as I know the committee is quite interested in the subject of regulation, these firms operate and are regulated in very different ways to banks, especially in terms of how their risk and liquidity is managed. Different regulation can be appropriate but, given the growth of this sector in the UK economy, as well as its interconnections with other parts of the ecosystem, it is absolutely right that the Bank of England and this committee are looking closely at it. I will end my introductory remarks there and I look forward to answering your questions.

Q163 The Chair: Thank you very much. Following up from that, could I just ask you about the proportion of your group's total lending you provide to private credit and private equity firms, and how much of it is international?

Michael Roberts: Yes, I would say more than half of it—probably 60% to 70%—is international. However, the overall size is actually quite small. Most private credit really began, and is in the largest form, in the US. When you hear the number of \$2.5 trillion quoted for private credit, that is more or less a US number. Our footprint, and therefore our exposure, is much smaller in the US.

The Chair: What is the number on quite small?

Michael Roberts: It is single digit billions and we have a \$3 trillion balance sheet, so it is quite small in comparison to their balance sheet.

The Chair: Could you tell the committee how you manage potential conflicts of interest that arise from the link between valuations, creditworthiness, and the volume of net asset value lending a private credit fund can secure?

Michael Roberts: Okay, I will unpack that question. So the NAV lending, which is the capital call lending, is really lent directly to the LPs; those are the investors who are investing into the funds. That is working capital financing, essentially, so we are lending against a timing difference between when the capital call occurs and when the LP can actually provide that capital to the fund itself.

There is not a conflict of interest and we are really basing our credit decisioning on, first, the strength of the LPs. These tend to be very well-rated investors, such as sovereign wealth funds, pension funds, large insurance companies, et cetera; and, secondly, the strength of the contract which, certainly in every instance that we lend, is a committed contract such that the LP must actually fund the capital call. That is considered a less risky part of the lending cycle for the private credit industry. There really is not a conflict of interest per se because we are lending directly to that LP, which is often a client of the bank as well. The general partner, the actual credit fund itself, is also always a partner or a relationship of the bank. But, in this instance, the credit per se is the LP interest credit.

Our other forms of lending would be to lend directly into the fund. That is what is typically called back-leverage. Back-leverage allows the fund to borrow from banks, for which they use the equity from the LP funds or providers, to then provide a greater amount of financing that improves their returns. The lending that we do then has direct call on the actual underlying assets of the fund itself. So it is secured lending with collateral that we analyse to make sure that we are comfortable with that collateral.

The Chair: Mr Dainton, what is your answer to the same question?

Stephen Dainton: We have about £20 billion in aggregate globally. That is roughly 5% to 6% of our lending exposure, to private credit, of which 70% will be evidenced in the US. As we have just heard, the US is the largest pool of lending of private credit and has been for the last 10 years.

From our perspective, not dissimilarly, you add some additional leverage with NAV lending that facilitates a number of things for a fund, as you might be aware, including not having to liquidate assets early. It forms some continuation of financing for the LPs themselves. Also, not dissimilarly, we lend to the GPs, which are substantial firms. Many of them are listed entities and some have reflected to this committee as well.

Q164 **Baroness Donaghy:** Mr Roberts, you mentioned the importance of interconnections, although my question is mainly for Mr Dainton. We have been told that the interconnections between banks and private markets are extensive. Can you provide an overview of the different types of private market firms, funds and portfolio companies that your group lend to, and what type of finance you provide? It has been reported that Barclays suffered a £110 million loss from the collapse of Tricolor. Can you explain how Barclays was exposed to Tricolor, and did this involve private credit?

Stephen Dainton: Yes. The exposure to Tricolor is a note of public record that Venkat announced during our Q3 earnings. That particular situation had a £110 million impairment on that lending facility. When you look at it in the context of our overall relationships with PE firms or private credit firms, no impairment is a situation that we should feel comfortable with. What it did was to absolutely cause a focus back on the strategy—the sourcing and underwriting capability and risk assessment of that particular lending capability—and, more than that, throughout the entirety of the portfolio. Again, during the Q3 earnings announcement, Venkat made it clear that he had initiated an extensive examination of the entirety of the portfolio before the end of the quarter.

In the process of assessing opportunities, we meet the management of the entity and very clearly assess the financial outlook and cash flow characteristics. Within that, you obviously have a number of covenants that you are capable of invoking, whether they are cash flow or leverage covenants that you are in control of, the liquidity management processes and, indeed, the personnel. There is a full due diligence process that we underwent with that particular asset. It has also been noted by Venkat and in the press that there is a potentially fraudulent activity that has taken place with that particular asset.

Baroness Donaghy: Mr Roberts, do you have anything you want to add on the general issue of interconnections?

Michael Roberts: I do not.

Q165 **Lord Vaux of Harrowden:** I have a question for Mr Roberts, just following up on something you said in your initial statement, if I may. You referred to the UK having the highest capitalisation requirements, which was restricting the abilities of banks to lend et cetera, and you went on to say that more needs to be done to allow banks to play a full role in the economy. Can you expand a bit more on what “more” would be, in specific terms?

Michael Roberts: Yes, and I will start with just the initial statement that high capital requirements are a cost to the bank because obviously we have to meet shareholder returns. The higher the capital, the more expensive that capital becomes and the more restrictive it is for us to lend out our balance sheet. And so it is a simple maths problem at the end of the day: the more capital, the higher the rates are, therefore the

more expensive and the less capital capacity or debt capacity we have to lend out.

"More" is in terms of looking at how we measure capital. Other jurisdictions are doing that today, as you know, which will put a competitive strain on UK banks, frankly, particularly when you look at what is happening in the United States. A difference already exists today between the UK and the US and, after the Basel 3.1 rules that will be issued in the US very soon, I would assume that there will be an even greater difference between the two.

The UK needs to look at where the US and other jurisdictions are going and look at what would be the appropriate capital structures and capital levels for the banks. I could certainly see either a lowering of the capital structures or the capital minimums. If you look at most of our global competitors, they run what we call a CT1 ratio at around 13%. We run it anywhere between 14.5% to 15.5%, which is 100 to 150 basis points above, so the most obvious thing to do there would be to lower the capital requirements. That would then allow us to lend more to the general economy and be able to do so at more competitive rates. As I mentioned in my opening statement, the ability for the private credit industry has really been greatly helped by the fact that expensive capital equals expensive pricing to middle market companies in particular, so we are much less competitive against those firms that do not have any of those requirements, either from a capital or a liquidity perspective.

I would say another issue is that the amount of liquidity we hold that we have mobilised on our balance sheet is quite considerable because of the liquidity rules that have been put in place; again, none of these other private credit firms has those types of requirements. The amount of money we could lend out is therefore restricted by high capital and high liquidity requirements, which mean less money going out the door for what is the mainstay of the UK economy. If we do lend out, it will be at higher rates in order to pay for our more expensive capital.

Lord Vaux of Harrowden: One thing that we have been told is that the risk weighting arrangements of different types of debt is much higher for direct lending than lending into private credit portfolios, which is pushing you into that kind of investment. Is that something that you recognise?

Michael Roberts: That is true 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. Because it is based on securitisation methodologies, you could lend a pool of different loans that are arranged by the private credit lender. We back-finance that lender, therefore we are getting the values of that diversification pool. However, 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. There is a considerable difference between lending into the private credit fund on that diversification and the securitisation basis, which is lending directly to the client itself.

The Chair: Could you just put some numbers on that differential?

Michael Roberts: Yes, it is 100% against the direct lending and 20% against the securitisation.

The Chair: So it is an 80% capital requirement?

Michael Roberts: Yes, it is a substantial difference.

Lord Vaux of Harrowden: Does Mr Dainton want to add anything, particularly to the more general question about what changes we could make to allow the banks to do more into the real economy?

Stephen Dainton: Mr Roberts has highlighted that there is a symmetry of global banking regulation, which is very important as the intention of Basel was to create that symmetry. When you have asymmetry, it creates anomalies in the system. Two things are very clear: first, there could be a direction of travel where one country moves away or slightly away from the Basel framework. It is extremely important that the UK watches the circumstances that evolve in the course of the next three months or so, certainly into the early part of next year, and ensures that, as a banking system in the UK, we are not disadvantaged if there are any changes towards regulation on a bank level.

The other thing I would acknowledge and recognise is that the scale of the private asset managers is material. Blackstone is one of the leading private asset managers on the planet, at around £200 billion of market cap; when you look at that relative to some UK asset managers, its scale becomes extremely important. It is also evidenced by a number of the other large listed private managers in the US: Apollo, and I would include BlackRock in that it already had private assets, but now it has acquired two very large private asset managers at scale and we should not underestimate that scale. In understanding that scale, it is important to reflect on whether the regulatory framework has to observe that in a more granular fashion, much like the banks are.

Obviously, post GFC, the banks saw a substantial level of regulation—appropriately so. From 2008, what you saw the banking system do, entirely appropriately, was to build its capital, as Mr Roberts has highlighted, to a core CET1 position that provides a material cushion in the event of a material stress. Many banks, ourselves included, have a 13.5% to 14.5% core CET1 target. It is important to recognise that the regulation put in place at that moment has actually allowed banks to get stronger. That in itself has now allowed banks to continue to lend very positively into the economy of the UK.

Lord Vaux of Harrowden: From your first statement, was there not a risk of a race to the bottom, effectively, if we all start cutting capital requirements and ending up back where we were in 2007-08?

Stephen Dainton: No, I would not necessarily say that we have to aggressively cut capital requirements. What I am saying is that we should ensure there is a harmonisation to global banking. If there is a

disadvantage to one geography versus another, it is likely that they apply their advantage in capital in extending their business models.

I do not necessarily think that it is a race to the bottom, in principle, because any time you extend risk—a loan is a risk; it is a risky thing that you do—you must meet certain criteria. I highlighted earlier whether that is a leverage ratio or cash flow ratio that you would want, the industry that it exists in is extremely important. We have to watch very carefully what changes are made—if they are—in a different geography.

Q166 Baroness Noakes: I am going to start pointing my question at Mr Roberts, mainly because I am drawing on what your CFO, Pam Kaur, said in connection with the recent Q3 earnings update. She was calling out the issue of private debt markets and said, “What is very important in these situations is to consider the second- and third-order risks”. She went on to say that the exposure of smaller lenders and hedge funds, “that we may be dealing with ... becomes a primary focus for us”. That implies that the impact of those smaller lenders and hedge funds in terms of overall risk had perhaps not yet been fully understood, which comes back to something that the governor has been talking about: effectively, the concentration risk.

How confident are you that, as a bank, you have a full understanding, not just in the primary impacts but through the second-order and third-order risks, of the impact on your bank’s balance sheet for the accumulation of these involvements in private credit?

Michael Roberts: That is a very good question. As Pam was saying, it is those second and third orders which, by their very nature, are much more difficult to really determine because they depend upon a series of consequences. As we look at them, it is not necessarily what happens if a private credit firm has problems, it is the consequences within the greater market and on other intermediaries in that market itself.

We are working at that all the time and we do a lot of stress testing just to try to see what those impacts would be; we try to look at different scenarios to make sure that we have as many different perspectives as we possibly can. I would say that we are never going to be in a position to have full knowledge of what every consequence would be because, by their very nature, that is almost impossible to do. However, we take a pretty conservative approach to the absolute quantum of direct exposures we have to the private credit players. We also look at where they themselves are lending: what segments of the economy where we would think the greatest difficulties would occur if there was a problem with a private credit company or lender, and we try to assess the impact that would have on us. Often those would be adjacencies. For instance, we are not lending to the company itself, perhaps that company is buying from other companies that we provide direct lending to. It could be a buyer to our suppliers; if our suppliers then cannot sell to the buyer, that obviously would be a second- or third-order event. It is about trying to look at that on a constant basis.

Clearly it is something that we will have to continue to do. In particular, as Mr Dainton said, this industry is big and will continue to grow. I would say that the growth rates that you have seen already of, say, 15% a year, will continue for the foreseeable future. There is going to be a larger percentage of the real economy that will be financed directly by these various private credit funds. As they occupy greater and greater space, we will have to see what the impact will be in the areas of the economy that we continue to lend to.

Baroness Noakes: Do you have enough information to establish the second- and third-order impacts?

Michael Roberts: It is difficult to get all the information. We know exactly what our exposure is, and what we can do is to look at various scenarios to try to ascertain what we think will be the impacts as it ripples through the economy. If I go back to 2008, I do not think anyone would have seen what the total impact was during that two to three-year period. So that is the difficulty: you just do not know how severe it will be or how widespread the impact will be.

Baroness Noakes: Mr Dainton, how confident are you about your risk management systems in Barclays to track not only the first-order impacts, which are probably fairly straightforward, but the second- and third-order impacts?

Stephen Dainton: Much as Mr Roberts said, there are extensive measures within our CRO—chief risk officer office—in and around your first-, second- and third-order risks. We measure and stress those extensively. To go back to what I said earlier, the awareness of bringing all the exposure together was probably prompted by the Bank of England two years ago, so I give our regulator and the Bank of England more broadly the credit for that. We knew where they sat individually but observing them all together and the tangential moving parts of each of those was important.

I would add that not only the scale of private credit and private credit managers, but the incentive to be private, is growing faster than I have ever seen. I grew up in the 1980s and 1990s in financial services where the listing process was your exit route. That clearly has changed post GFC, and the incentive to exist in a private world as a corporation is evidenced by the number of listed corporations that we see here in the UK and, indeed, in the US; you have a confluence of factors.

The pool of available assets that private capital can find is going to continue to grow unless there are material changes in listing requirements. If you are a new or a younger corporation, some requirements around being a listed company feel very onerous. If your entire intention is in growth mode, you do not necessarily want to come back to the market and explain a three-year strategic direction every single quarter. The Bank of England is getting ahead of this in understanding some of the major structural themes that are changing in our ecosystem; it does not mean that it is wrong at all, but those

changes mean that the scale of assets will grow, and the scale of potential investable assets will continue to grow as well.

The Chair: That is a really important point which might be a future topic for this committee. Lord Sharkey, you wanted to come in.

Q167 **Lord Sharkey:** I just wanted to follow up on those two answers: what can or should be done to increase transparency in the private sector? What place is there, if any, for additional regulation?

Michael Roberts: Are you asking about regulation of the funds themselves?

Lord Sharkey: Yes, but also about the regulatory landscape in general.

Michael Roberts: I will try to answer both your questions. First, on transparency: the funds—I have read their own testimony—understand that they need to produce much greater transparency. That is probably something they need to do for their own LPs, their own investors, who clearly should have that information.

However, as Mr Dainton said, the nature of the industry is that more companies want to stay private. Private means they do not have to give out information, and they do not want to, so there will be a bit of push and pull here. It is certainly preferable to have much more transparency and much more information because they occupy such a large part of the economy today, both here and elsewhere, particularly in the US. If there were a big adverse development, US policymakers and regulators would need to know what they were dealing with—therein lies the problem. Short of forcing them to give that information, they will not necessarily provide it because that is the benefit, again, of being private.

The LPs are willing investors; they understand the risk they are taking. In order to deal with the issue, the regulatory bodies would have to decide to regulate this asset class. Notwithstanding the fact that there are no depositors, they would need to use some of the same tools as they do with banks and approach it in a similar way to some degree. So that would probably be the major action to take.

In terms of regulating the funds, I know many regulators have looked at this, but they do not necessarily know the best way to do so because of the fact that these are private investors investing in private assets. They have the ability to regulate, but would need a much more extended justification given that there is no direct public investment by investors who need to have the information to make those types of investments. It is a quandary.

If, however, you could get over that philosophical hurdle, you could require information on the type of assets they are investing in, the concentration of those assets and the overall tenure of the loans that they are making. That would at least give you a better idea today of what would happen if there were a very adverse event. I would probably start

out with that type of approach, should the regulatory bodies decide to regulate them in any way, shape or form.

Stephen Dainton: I would agree with Mr Roberts. In particular, the delineation of a bank is that it has depositors' money. We are stewards of our depositors' cash, so material losses could potentially impact that.

These are very talented asset managers who have grown over the course of the past 20 to 30 years, and we have to acknowledge that. However, we also have to acknowledge, as I said earlier, that the scale of these asset managers is very large, north of \$1trillion or \$2 trillion of AUM. I do not necessarily believe that they are a systemic risk as the banking system could be; the regulation has to be tailored to understanding the scale of the asset managers themselves and the fact, as we both reflected earlier, that there will be a continued growth in private need for capital because there will be a greater number of private assets to invest in.

Q168 **Lord Hollick:** Picking up on the last two comments, it seems to me that the banks are at a competitive disadvantage: you need to provide more capital and more liquidity to increase your book of lending. Mr Roberts, you mentioned that private credit is growing at 15% per annum, which I guess is rather larger than the banking business is growing at the moment. Would it be possible to compete in that market by setting up stand-alone private credit funds? If you can use your ability and relationships with a large number of borrowers to provide credit to what is apparently a very hungry market for private credit funds, is the risk distributed to the LPs rather than in your balance sheet?

Michael Roberts: We essentially do that today. We sell and have an ongoing relationship with many of the credit funds that have been mentioned; through an originate-to-distribute approach, we take loans off our balance sheet and sell them directly to the private credit funds themselves. For regulatory reasons, we do not set up funds ourselves; that is prohibited under the Volcker Rule and other rules that were put in place following the financial crisis. But we can clearly use those funds to take a lot of our exposures that are not suited for the banking system or where we just need to diversify our loan portfolios for risk and return reasons.

I will give you one example: infrastructure loans. They typically have very long tenures because the projects themselves are of long duration. Such loans are an asset that is much better held by these private credit funds than by a bank given how the capital regimes work. A long tenured loan of that nature is, frankly, too expensive for us to hold in our own balance sheet; we will never generate the returns necessary to pay for that loan, so we often package them together and sell them to the private credit funds themselves. In fact, they like these types of investments. Many of these funds today have insurance companies, so they have long-term liabilities and are looking for long-term assets. The insurance sector is a more preferential place or type of entity to place these types of loans. We can therefore use the private credit industry to

help us mitigate our risk, to us get the returns for the loans ourselves, to manage our capital and to allow us to recycle our own balance sheets such that we can lend additional monies to the real economy.

Lord Hollick: You could indeed lend the private credit funds quite separately as well, to give them leverage.

Michael Roberts: Yes, we could do that as well.

Stephen Dainton: I reflect that, a year and a half ago, our CEO laid out a very clear strategy for the UK, providing £30 billion of additional RWAs into the UK over a three-year period. We have a business prosperity fund that is dedicated to SMEs, at a £22 billion scale; we have allocated £10.5 billion of that during the course of this year, which is up by 42%. We are actively lending into the SME sector already and helping private asset managers lend by fund or direct measure as well. I would agree with Mr Roberts that the banks, certainly here in the UK, are actively lending into the SME sector and will continue to do so.

One thing I would say, however, is that the demand for that capital is, and has been, somewhat muted. Corporations here in the United Kingdom should be comfortable borrowing debt to grow if they have confidence in the circumstances ahead of them, including confidence in regulation and confidence in the business environment. Again, I come back to the growth opportunities in the UK. We do not have the tech scale that the United States has, and we should acknowledge and recognise that, but we do have a significant opportunity to grow. Both of us here are in the financial services industry, which is uniquely talented. We have incredible schools and universities, and we have incredible regulators at scale. Here in the UK, we have asset managers at scale, banks and insurance companies at scale to grow. Because of our talent pool—even in the post-Brexit environment—our banking system, certainly the City of London, has demonstrated a resilience to continue to be a material part of the UK's armoury when it comes to industry.

I certainly know from my CEO, Venkat, that there is a huge commitment to lend, and it is our intention to continue to do so.

Q169 **Lord Kestenbaum:** Could I stay with that point, please, and press you both a little on the evidence that we have taken thus far about demand, from SMEs in particular?

Mr Dainton, you spoke about muted demand. At the same time, a good body of the evidence that we have picked up—Mr Roberts, you referred to this—is that a combination of higher capital liquidity requirements, conduct requirements and other aspects of the regulatory framework that raise the cost of capital and in turn make those costs transferable to the customer, is a primary contributor to the so-called muting of demand. I am aware that there is a classic backwards and forwards discussion; often the suppliers of capital will say, "We're desperate to borrow, but there's muted demand because there's insufficient ambition", and those who are aiming to borrow say, "We're desperate to borrow, but the cost

of capital and the risk appetites of the lenders don't allow us to".

I wonder where you both come out on that dilemma.

Stephen Dainton: I would reflect that, between 2012 and 2024, the application for demand of debt among SMEs declined by 50%. It is a huge focus of attention for the lending institutions here. Actually, it has been a huge focus of attention since Macmillan in 1931, with a focus on SMEs; that is critical. There has been a decline in the demand but it is also a factor of available financing, whether that is VC financing in equity form, or in private equity form, not necessarily just debt. The characteristics around how we allocate and lend in debt form to SMEs become incredibly important.

Lord Kestenbaum: Let me make my question more acute. What is not in question is the dramatic fall in demand; obviously, the data points to that. I guess my question is sharper than that: where does the resolution lie? Is it unambitious entrepreneurs, or a regulatory framework that is imposed upon institutions like yours, which makes it commercially impossible to meet the entrepreneurs' requirements?

Stephen Dainton: If we take a look at the entirety of the ecosystem in capital formation, which is really important, and take the United States, for example: it exhibits exceptional capital formation from early stage VC. In fact, in the UK we also do a pretty exceptional job of providing early stage capital, but where we are probably lacking is in the scale-up process. From my perspective, that should be a focus of attention for us and—as you walk through that scale-up—so should be the exit route. So that becomes your exchange: the liquidity that is provided in an equity market. There have been a number of comments in the course of the last two years on the scale of the UK equity market and our ability to bring new corporates into that environment for listing.

It is a multitude of different things, including capital formation, the regulation around your lenders in all forms, and ensuring that, certainly from a banking perspective, your depositors are safe. That is important. We have a ring-fence bank in the UK; that is extremely important. Financial stability is aided, and we should applaud that, post GFC; despite Covid or the Russian war with Ukraine, which caused some dislocation in other countries—

The Chair: Mr Dainton, this is a very simple question, which is about whether the regulations are making it too expensive for small firms to borrow from the banks. Is that the case or not?

Stephen Dainton: There are some situations where that could be the case. It depends on the asset. Sorry.

The Chair: Thank you. Mr Roberts, do you want to comment on that?

Michael Roberts: I would agree. Most of our SME lending is done in our ring-fence bank. Frankly, the ring-fencing itself adds a lot of expense to running a bank so I would say that is something to be looked at. Clearly,

it has an impact, though. If the cost of capital or cost of liquidity is more expensive, it will clearly have an impact. It is not the only factor, but it is certainly a very important factor.

Q170 The Chair: I know you have to go at 10 am but, just on this point on capital, one thing we have had in evidence is that the banks complain about the capital requirements and the 2% additional burden that applies relative to European banks and others, but they never use their buffers. The reason they do not use their buffers is because they are worried about the signals that would send to the market; they are uncertain as to where the regulators are coming from on the buffers and they fear that they might be caught out. Is that a fair comment or not?

Michael Roberts: That is a fair comment. Buffers—both liquidity and capital buffers—are there to not to be used. We have multiple layers of both and it is quite inefficient, to be honest. If I were running the bank only for efficiency, I would not have them. 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.

The Chair: What is the remedy for the regulators then?

Michael Roberts: If you have faith in your capital and liquidity regimes, you should not need buffers. But we have said that, even though we have these expansive capital and liquidity regimes, we want buffers on top of that. We have to draw the line and say that we have faith and confidence that we have the proper regimes and we do not need to have buffers on top. That has not been clearly defined and spelled out by the regulators. However, it is not just down to them; it is also due to overall market perception. It has become a hardwired part of how banks are perceived and judged and assessed from a credit perspective, and that is the fundamental issue for banks. We have needed to have a very strong balance sheet and going forward, we have to redefine the credit worthiness of a bank.

Q171 Lord Grabiner: I also want to ask you about capital and liquidity requirements. Both Barclays and HSBC are worldwide, and you of course face a variety of regulators in the Far East, in the States, in Europe, presumably, and certainly in the UK. In big-picture terms, how do these requirements get set? Is there a negotiation? There must be a negotiation with regulators. To what extent is it imposed upon you in the light of what you are telling them, or are you able to give a pretty powerful indication to the regulators of what those requirements should be? I find it quite difficult to bottom this out.

In particular, I have in mind Mr Dainton's symmetry and asymmetry point. What is the answer to that question? In other words, how is it that these limits get set? To what extent are they the result of what you are saying to the regulator, or what the regulator is saying to you?

The Chair: Mr Roberts, we will start with you because I know you have to go shortly.

Michael Roberts: Unfortunately, there is no harmonisation among regulators. Basel III, as Mr Dainton said, was supposed to harmonise the system but for various reasons it has not turned out that way. We have many regulators, as you would imagine—57 of them—but there is a group of 20 lead regulators and a super group of four or five principal regulators. Our primary regulators, obviously, are the PRA and the FCA.

There is divergence, certainly today, and there will be more and more divergence. We do not necessarily have negotiating power so we have to abide by the regulation in each country in which we operate. We hope that there are similarities, but our standards are set at the highest regulation on a global basis. That means that we may have regulation that is even higher than the PRA would require us to have. If that regulation is such then we have to operate it and it is key to our operations that we operate with that regulatory standard on a global basis.

Our “know your customer” anti-money laundering system is a good example of that. For many years we have operated under US standards that are historically the highest. We have imposed that on a global basis because we send payments all around the world; in fact since we are 75% of a US dollar bank, we have to operate under US standards. However, there will be other parts of the regulations that we have to borrow, whether from the PRA, HKMA, or the US regulators as well.

One challenge for any global bank is that you have multiple regulatory bodies you need to focus on, and you have to be able to operate in a world where there are often different answers for the same regulation. That is just one of the challenges of a global bank that you have to be able to manage.

Stephen Dainton: I would reflect something very similar. The core college, as groups of regulators, has active discussions on this, and the Basel committee has active participation from banks and regulators. There is ample room for consultation and dialogue; they undertake that and so do we. Within the framework that we operate we also have to ensure that we are adherent to a number of global regulators with capital add-ons at the determination of any one of those regulators.

Lord Grabiner: Are you happy with the current structure? I can see that it is a straitjacket and there is not a lot that can be done about it.

Stephen Dainton: Basel III was intentionally set up to create harmony across bank capital regulation. I would encourage us to operate in that environment to the extent that we can have a representation to get us to that place.

Q172 **Lord Eatwell:** I want to discuss some instruments that have started to appear in the development of the private credit market. Mr Roberts has already referred to the origination of obligations, their sale onwards in terms of various collateralised funds, and the building of that structure within the market. We have also been told about the development of

significant risk transfers, which is a notion the other way where you can sell on the risk in the particular portfolio held by the bank of funds going into private equity and private credit. Now, these instruments are very reflective of the instruments we saw in the global financial crisis. Collateralisation, selling of tranches, and so on, was something which characterised that; significant risk transfers are just another form of credit derivative.

I will ask Mr Roberts first because he has to go: you have talked already about moving particular assets off your balance sheet by selling them on into that market. Are these sold through collateralised instruments and selling tranches on collateralised instruments? On the other side, do you use significant risk transfers to reduce the risk of the portfolio you hold?

Michael Roberts: The answer is yes to both questions; we use SRTs, sparingly, and we are certainly not the largest user. By the way, SRTs have been around since the late 1990s, and were primarily used by continental European banks. They came to the UK and the US a little later. We use them, we have used them before and we use them on various parts of the portfolio. To your point, they are a derivative but they are used on a portfolio basis. Although there is risk sharing, we share the risk with the ultimate buyer. They are essentially buying the second layers or the latter tranches, if you will, of potential losses.

The reverse of that is the CLOs, which you mentioned as well; we have done CLOs and will continue to do them. CLOs also use the tranching securitisation technologies you mentioned. The difference is that the equities brought in by the CLO manager will probably be 12% or 13%, and then different tranches of debt are put on top of that. Both are effective tools. Both are used really for risk management purposes, and in particular for concentration risk purposes; we do not want to hold too much of, say, a certain industry or a certain company. You are essentially buying insurance and it is a very healthy part of an overall portfolio management approach.

As I mentioned earlier, we also supplement by selling loans directly to various buyers, often credit funds themselves. I know you referenced the earlier use of these instruments: the amount of leverage that was in the system before and the much less rigorous underwriting standards. Most of what we saw in the past were CDOs, which are mortgage-backed securities and essentially very similar. The CDOs themselves were not the problem; there was too much leverage in the system, which they compounded and often amplified, and that was really where the problems arose.

We are taking a much more cautious approach, and the industry is taking a much more cautious approach. These are actually a good way for the banking system to actively manage its loan portfolio so that we keep excessive risk out of the banking system. We allow it to go into the non-banking system, but on a very diversified basis.

Lord Eatwell: Both these instruments are based on probabilistic analysis

of what has happened in the past. Therefore, they are very tied to the experience of the past; that is how the models are built. If the future is not like the past, that is when things blow up and go wrong. Could you reflect on Barclay's use of these instruments today, Mr Dainton?

Stephen Dainton: Yes; in a not dissimilar way, we have an SRT programme that effectively extends to the first loss absorption for our portfolio. We finance CLOs, but not to a substantial degree. If we look at the credit worthiness of those, 80% of our exposure will be in AAA and, of that, 75% to 80% will be in the US. We use these instruments in part as risk mitigation for the firm; we should and will continue to do so.

As it relates to the forward-looking or historic-looking action in the models, risk models are becoming significantly more dynamic in anticipatory events. Obviously, we run material stresses into the portfolio, which takes a moment in time and an event. Now we are able to bring into that environment a much more dynamic assessment of the forward-looking event.

The Chair: On that note, I thank you both for answering our questions, and you in particular, Mr Roberts, for giving us an extra 10 minutes of your very busy life. That concludes the public part of this session, and we are very grateful to you both for coming to support us.