HOUSE OF COMMONS

Treasury Committee

Oral evidence: Economic impact of Coronavirus, HC 271

Wednesday 15 April 2020

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Watch the meeting

Members present: Mel Stride (Chair); Rushanara Ali; Mr Steve Baker; Harriett Baldwin; Anthony Browne; Felicity Buchan; Ms Angela Eagle; Julie Marson; Alison Thewliss.

Questions 152 - 229

Witnesses

I: Stephen Jones, CEO, UK Finance; and Stephen Haddrill, Director General, Finance and Leasing Association.

II: Sam Woods, Deputy Governor Bank of England and CEO of the Prudential Regulation Authority; Sarah Breeden, Executive Director UK Deposit Takers Supervision, Prudential Regulation Authority; and Christopher Woolard, Interim CEO, Financial Conduct Authority.

Examination of witnesses

Witnesses: Stephen Jones and Stephen Haddrill.

Q152 **Chair:** Good afternoon, everybody. Welcome to the Treasury Committee and our latest session on the economic impact of the coronavirus. I particularly welcome our two witnesses in the first of two panels this afternoon. Will the witnesses introduce themselves very briefly, starting with Stephen Jones?

Stephen Jones: My name is Stephen Jones. I am the chief executive of UK Finance, which is the trade association that represents about 270 banks, building societies, credit card companies and payment service providers across the UK. We act as a convenor across that industry, with expertise in relevant underlying markets—wholesale, retail, commercial, payments—and we have been working closely through the crisis with our members, regulators and Government as the responses to the crisis evolve.

Stephen Haddrill: I am Stephen Haddrill, director general of the Finance and Leasing Association. We represent 166 finance houses in the personal lending area, lending to SMEs through leasing products, and motor finance. All total new lending each year is about £140 billion, and about £200 billion in total at the moment.

Q153 **Chair:** Thank you both very much, and welcome to the Committee. We will move at some pace through this session because we have two panels, so I ask our witnesses to answer as succinctly and briefly as possible. For most answers, let us work on the assumption that perhaps just one of you will answer, so if you are particularly keen to answer a question, raise your hand. For those who ask the questions, if they could be directed to one of the witnesses, if possible, that would be great.

I will start with a question to Stephen Jones. Information we received today is that UK Finance is saying that the loans going out at the moment total £1.1 billion, which is 6,000 successful loans out of 24,000 applications. On the face of it, that sounds encouraging, particularly given that we started at a very low level initially, but when we look at places such as Switzerland, where 18,000 companies are being helped in this way, or Germany, where they seem to have got out about €7 billion-worth of finance in this way, we still appear to be lagging some way behind where we could and should be. I would value your comment on that.

Stephen Jones: The data that you quote—£1.1 billion and 6,000 loans deployed in the three or so weeks since the CBILS has been put out there—is correct, as is the number of applications that have been made, now 28,000, so just over 20% of loans applied for to date have been granted. I point to the fact that the CBIL scheme as designed by the UK

Government is a very different one from the German and Swiss schemes, which are both 100% guaranteed schemes. In that context, therefore, the credit assessment required by banks in deploying the money is much simpler. In the UK scheme, we have to decide as banks, as participants in the scheme: was the business viable on 31 December 2019? Does it have the capability, after the crisis, to repay the debt that it is proposing to take on? Is there security that it can make available to support the loan?

Since the clarifications to the scheme announced by the Chancellor on 3 April, it is clear that all viable businesses now are able to access the scheme. Previously, those businesses who could have borrowed on arm's length commercial terms were required to do so, and were denied access to the scheme. In that context, following the three weeks that we have had to deploy, we would like to see a bigger number; we are working extremely hard to increase it, and it is in everybody's interest for every viable business that falls within the rules of the scheme to receive financing under the scheme as quickly as possible. All the accredited members under the scheme are doing everything that they possibly can to make that happen.

Q154 **Chair:** Thank you. You said you would like to see it bigger—we would like that, too. Do you have a number that you could put on that, for a week's time, two weeks' time and three weeks' time?

Secondly, you mentioned the 100% guarantee situation. That would bring with it some element of moral hazard: if banks have no skin in the game and are not at risk at all, and they are playing with taxpayers' money, can one expect them to behave entirely responsibly? Do you recognise that problem? How much of a problem do you think that would be if the Government introduced 100% guarantees?

Stephen Jones: I recognise the problem. In identifying a scheme where the Government are guaranteeing 80% and are requiring firms to undertake credit assessments of proposed borrowers on the way in to the scheme, the Government are expressing a very different risk appetite and parcel of businesses that they wish to support under the scheme than is being expressed for smaller businesses in Germany and Switzerland. There, a risk decision has been taken—they want everybody more or less that was viable going into the crisis to receive that money, and they want them to receive it fast. That is not the decision we have taken in the UK; that is a decision for Government to take. We work within the rules of the scheme as they currently exist. Banks have 20% risk exposure; they are also required to assess the Government's 80% risk exposure on the Government's behalf in making the credit assessment that I mentioned in my answer to the previous question.

Were the Government to want to support more businesses, including those that might not otherwise be able to repay debt after the crisis, it might be possible to change that guarantee level in the scheme. Banks would then not be required to undertake a full credit assessment. But I recognise your analysis of the moral hazard that that represents. There will be more unsuccessful businesses that are able to access credit under the scheme, and possibly a greater risk of fraud. It is possible that we need a combination of the two: at the very small end of the SME market, perhaps loans below £25,000, where there is huge volume and probably the biggest backlog, making the scheme simpler for that kind of borrower might be a solution that we would look at. I would urge a few more days of patience, as we see how the data pan out and how much more we are able to deploy at pace, before any re-engineering of the scheme is done.

Chair: Thank you. I am aware that Stephen Haddrill would like to come in, but I will pass to Alison Thewliss. Alison, to the extent you can, perhaps you will bring in Stephen.

Q155 **Alison Thewliss:** The FCA is mandating a package of relief for households, including three-month repayment holidays on loans and credit cards and £500 interest-free overdrafts. Can you tell me whether the industry supports these measures and the mortgage holiday agreed with the Treasury? Will they go far enough to prevent households from experiencing financial distress?

Stephen Jones: I am happy to take that. We came forward with the mortgage support measures about four weeks ago: 90 days of payment relief for households who come forward seeking that relief. As we announced yesterday, 1.2 million customers have come forward requesting that relief, which is about one in nine mortgage borrowers across both the owner-occupier and buy-to-let markets in the UK. We are very supportive of those measures, just as we are supportive of the package of measures around unsecured credit—overdrafts, credit cards and instalment loans, which the FCA announced, having worked with us for a couple of weeks to get the regulation and legalities of that right. They are now being deployed as of yesterday by all providers of consumer finance.

We think it is absolutely the right thing to do to give as much flexibility as possible to households and businesses to manage debt, to have the opportunity to manage their cash flows through this crisis. Those payment holidays are a very good way to do so for those who need it. I would, however, stress that not every household or business needs a payment holiday, and those payment holidays do roll up, so the repayments that are not being made will need to be made once the holiday is over. This is not a write-off. Only those customers who are already in serious financial difficulty have the opportunity at this stage to have their interest written off and capital repayments suspended, and those normal forbearance measures that existed before the crisis continue to apply.

Q156 **Alison Thewliss:** Will that be long enough?

Stephen Jones: Is 90 days long enough? I don't know; I don't have a crystal ball. That is a matter for public health experts, the Government, and those of us who are trying to predict at what pace and at what point we come out of the crisis, such that household and business cash flows return to as near as possible to what they were before the crisis. I have no doubt that that is a decision that will need to be reviewed in June.

I would point out that the financial institutions only have finite resources in terms of the number of holidays they continue to roll. It is very important that households and businesses understand that the reliefs that are given must be temporary, and there will come a point where those payments will need to be restored, if you like. However, you are right to point to whether the timing is enough. I honestly think nobody can answer that question at the moment.

Q157 **Alison Thewliss:** In terms of missed payments—this might be more of a question for Mr Haddrill—is there any information about how your members are reacting to missed payments, and missed payments without prior agreement being reported to the Treasury and its agencies?

Stephen Haddrill: Yes, absolutely. I didn't quite catch the question entirely, so if I don't get it quite right, perhaps you can have another go.

We have been surveying our members regarding the number of people who have been applying for some kind of payment holiday or other support, and as of Friday 3 April, they have had about half a million applications for some form of support. By that date, over 300,000 had been given the support they were looking for. The gap is really people who remain in the pipeline either because the firm is awaiting their approval of what has been offered, or because a bit more information is needed. As Stephen Jones was saying just now, there are some cases where the three-month holiday is not necessarily the best thing for the customer, particularly if they are already well in arrears. It may need a longer restructuring of the debt or something like that, which requires a conversation, but I entirely agree with him that the three-month approach is the right one.

What I would say is that we need to work out what happens after three months, before June. I think the scenarios need to be developed now, not least because—as Stephen said—resources are finite, and we do not want to get to the end of the three-month period with just an assumption that there will be another three months or whatever. There needs to be some serious modelling before we get to that point.

Alison Thewliss: My time is up, so I will pass on to the next person.

Chair: Thank you very much, Alison. We move now to Felicity.

Q158 **Felicity Buchan:** Thank you. As I see it, businesses are looking for three things from the banking sector. They are looking for sufficient capacity; they are looking for quickness of turnaround; and they are looking for the loans to be on reasonable, non-exorbitant terms. Do you think the banking sector is delivering on those three criteria?

Stephen Jones: I do think the banking sector recognises that it needs to be the transmission mechanism for the solution in this crisis, that it is not part of the problem in this crisis, and that it has an opportunity to make good some of the ills of the past. I see behaviour day in, day out that is designed to support customers, whether through the rapid deployment of CBILS—as rapidly as it can be deployed, given its terms and the speed at which it was required to be engineered—or through other measures. Those include lending to borrowers who are not eligible under CBILS, normal payment holidays and forbearance being shown to existing borrowers in respect of their existing debt, and advice when it is required by businesses to decide what the best course of action is.

What the vast majority of businesses in our economy are enduring at the moment is a horrendous shock to our economy and to those businesses. The banks very, very much want to be seen to be, and to act as, part of the solution to make that shock as manageable as it possibly can be. I would, however, stress the remarks made by the Chancellor—that not all businesses will survive this crisis. There were businesses that went into the crisis that were not strong. In a normal year over the last five years, around 12% of all businesses have failed and been wound up. We need to ensure that we are engineering solutions that give the greatest chance to the greatest number of potentially viable businesses, and which give them the opportunity to trade through and trade out of this crisis when eventually the recovery comes. I am absolutely convinced that the industry is doing everything it can to make that happen.

Q159 **Felicity Buchan:** And do you think that the banks have the operational capacity to turn around the volume of requests? I am clearly aware that banks are not working with 100% staff in their seats, and that people are working from home. Is the operational capacity out there?

Stephen Jones: You point to a constraint on every business operating in the current environment. We are very grateful that the Government conferred key worker status on banks, so that the workers who need to be in branches, call centres and technology centres are able to be there in order to ensure the greatest level of operational capability possible. But you are right to point to the fact that there is, on average, a 30% absentee rate at the moment, for illness reasons and for caring reasons; workers have their own family needs. Frankly, the frontline staff in branches and call centres are putting themselves in the line of fire and increasing their own risk in doing so. With all that said, thousands of bank workers were working over the weekend—through the Easter holidays—to try to get through the CBILS backlog. There will be an enormous uplift in volume from customers seeking consumer credit forbearance as a result of that taking effect yesterday. But the fact that we have been able, for example, to mobilise 61,000 mortgage payment holidays a day every day for the past three weeks demonstrates that, notwithstanding the operational constraints, the banks are doing everything they can to do as much as they can as fast as they can.

Q160 **Felicity Buchan:** I have heard that only two banks are offering essentially overdraft facilities under the CBIL scheme. Would you like to see that extended, with more banks providing those facilities?

Stephen Jones: There is a problem for some banks who were not previously active in the sub-£25,000 loan range—whether that was a term loan or an overdraft—in mobilising themselves to do so. From a regulatory and legal perspective, it is quite a complex space to operate in. If you were not operating at that size of loan on the existing British Business Bank operational rails, it is quite hard to set that up safely. There are significant conduct penalties for getting that wrong at the smaller end, and, believe it or not, the Consumer Credit Act also applies to smaller businesses.

Many small businesses at the smallest end have not borrowed, historically. If you have banked a business customer for many years, but that business customer now comes to you to undertake a loan for the first time, you also have to undertake full KYC—know your customer—checks on your customer for the first time. Those are all aspects of our regulatory and legal framework, designed in peacetime to protect small businesses and to ensure that they can navigate the financial system as safely as possible, that actually cause some difficulty in deploying quickly and at pace today at the smaller end of the market, which you point to.

Q161 **Felicity Buchan:** I have just one last quick question. I have heard that certain big banks are just refusing to lend to certain sectors—for instance, financial services. Is that your experience?

Stephen Jones: I can't comment specifically on financial services. I represent a number of non-bank financial services providers who are a critical part of the system and who do need financing. Many are financed through bank lines and then inter-securitisation structures, and those funding structures are not working at the moment because the underlying markets are not working. We are in very detailed discussions with the Treasury and the Bank of England to try to design a scheme that will enable those incredibly important credit transmission mechanisms—often to underserved segments of the consumer and SME market—to continue to operate, because we need them to operate coming out of this crisis.

I do recognise this somewhat. I wouldn't say that it is banks not lending to non-banks; I do not recognise that construction. But I do recognise that for non-bank specialist finance providers who rely on wholesale funding, their funding models are not working at the moment.

Chair: Thank you, Felicity. I am now going to move on to Angela.

Q162 **Ms Eagle:** Mr Jones, do you think, given your experience to date, that the coronavirus business interruption loan scheme is actually too complex to achieve its aim, which was to save businesses forced to shut because of the lockdown?

Stephen Jones: I'm not sure that was the aim, given the terms on which it was deployed. I think its aim was to save viable businesses that have an opportunity to survive and that will have the capability to repay the debt that the civil scheme requires them to take on. That is certainly the scheme that we have been asked to deploy.

I think that if risk appetite is greater than that and the Government wish to provide greater means for more businesses to survive the crisis, then potentially the scheme could be made simpler, and it could be made a little more generous, in order that more businesses have the opportunity to survive.

However, I do believe that within the parameters of CBILS, given the time, it will be shown to succeed, particularly for mid and larger SMEs. At the smaller end of the SME market, where, as referenced, there are operational difficulties, we are working very hard to deal with as many as we can in as automated a fashion as we can. However, that is difficult, and the scheme is not the same as the equivalent scheme, for example, in Germany, which is called Schnellkredit. That was actually launched today, with 100% Government guarantees for the smallest of SMEs.

Q163 **Ms Eagle:** Do you think that it is really possible to define, in such unprecedented circumstances, what a viable business is, when the Government have, for the very understandable reason of saving lives in an unprecedented global pandemic, effectively told the economy that it has got to be on hold? How on earth do you decide what a viable business is in that circumstance?

Stephen Haddrill: That's an historical judgment, I think, rather than a forward-looking one. If the business has been successful up until now, I think it is worthy of support, rather than trying to use a crystal ball to identify what is coming up. And that is why—

Q164 **Ms Eagle:** Do you think that that is the judgment that those who are administering these schemes are actually making now? I think that all of us, as MPs, are getting correspondence from our constituents and from businesses more generally that regard themselves as viable but have been told that they're not by those they are seeking to get these loans from.

Stephen Haddrill: I think it's a judgment they should be making, and I think on this point about a 100% guarantee, or another option around the totality of borrowing under CBILS, the guarantee is only 60% at that level, if you aggregate everything together. So, I think that should go up, as well.

Whatever we can do to reduce the credit risk associated with that lending, the better, and the less likely it is that big banks maybe take too harsh a position. I certainly think that they should just be looking at the success of the business up until then.

The other thing is that, as Stephen said, there is this big non-bank sector that the Finance and Leasing Association represents. It is very keen to lend, but it is having trouble accessing the capital markets in order to take forward that lending. And of course, in many cases the FLA has very long-term customers, so they are able to form a judgment about those customers—there are also some quite deep relationships—and they will want to keep them alive. So, I think this non-bank issue is a really important one, and we need to have the schemes widened, speeded up and so on, so that they can be brought into the mix.

Q165 **Ms Eagle:** And is the bottleneck the British Business Bank and its capacity to accredit new lenders?

Stephen Haddrill: It is an issue about the speed of accreditation. They have put a lot more people on.

Q166 **Ms Eagle:** I think they had two originally—stunningly—and they now have 25. Is that what is going to save the British economy?

Stephen Haddrill: No, I think they need to go further. Our members have offered to give them staff to help—trained underwriters who could support them. I also think the process needs to be looked at. It is not just about new people. It is about whether the governance around decisions being taken—which, to use Stephen's earlier phrase, is a peacetime process—can be speeded up; that ought to be considered. There are other things. The term funding scheme from the Bank of England for SMEs flows into the banks. It does not flow into the non-bank sector, so we need something similar for the non-bank sector.

Q167 **Ms Eagle:** One final question for Mr Jones. Do you think that the interruption scheme that you have been asked to administer would have been better if it had been more generous? You talked about 100% guarantees from the Government. Do you think that that would have been a better way forward?

Stephen Jones: With the benefit of hindsight, that is a crystal ball we did not have at the time. I think the Chancellor, the Treasury and the British Business Bank came up with the right scheme in the circumstances. They have acted very quickly to change the terms of the scheme as they have seen how it has been deployed. There remains a gap for businesses that were not profitable at the end of 2019 and/or businesses that are unlikely to be sufficiently profitable at the end of this in order to be able to sustain the debt they need to take on to survive. Those businesses are not catered for under the scheme. That gap exists, and we need to decide collectively what we do about it.

Chair: Thank you, Angela. We will now go to Rushanara.

Q168 **Rushanara Ali:** Thank you very much. Mr Jones, I want to pick up on the points that have been made. In terms of the broad thrust of what you are saying, what is your sense of how small businesses are ultimately being treated? If we take the long view of how small businesses ended up suffering in the last financial crisis, you spoke about survival, and it feels like there is a narrative—it is not your narrative—of survival of the fittest, but the impact on different groups of businesses will be different. Larger businesses—quite understandably, because of strategic interests—are going to get more help faster. They will be able to overcome some of the barriers you mentioned.

You touched on the 100% guarantee. Can you be more explicit? Should the Government make a strategic decision about saving those small businesses, particularly the ones on the frontline that are essential to our communities? Do you think the Government should step in and support them, at least for the foreseeable future, because they did not start off with a level playing field and this is exacerbating those inequalities? Do you think the Government should take action now, in the light of what you and your colleague have said?

Stephen Jones: First of all, the SME community and the smaller end of the SME community are the vital backbone of business in the United Kingdom. I think they will be absolutely critical to our successful emergence from this crisis, and I believe that we should do everything we can to provide the support that enables that economic capacity and enables the personal and social issues associated with businesses failing to be avoided as much as they possibly can be. Where you define the limit in terms of businesses to support and not to support is ultimately, in the current circumstances, a matter for Government, rather than for me as a spokesman for the banking industry. The banking industry will do everything it can to support as best it can, within the parameters that it has. Ultimately, banks are lending depositors' money, so unless there is a measure of support for greater risk appetite and trying to get the money back at the end of the crisis, they cannot lend to businesses that they perceive to be likely to fail through the crisis.

Q169 **Rushanara Ali:** Basically, your message to Government is—I am putting words in your mouth—"Get your act together on this essential section of our economy, which employs millions of people, and banks will step in and address it, but don't attack banks when we are doing the best we can in the circumstances." Sorry, I know that those are my words, but is that essentially what is happening?

Stephen Jones: I would never say, "Government, get your act together." We are in unprecedented circumstances, and the range of measures that has been introduced not just in lending but in rates and jobs is incredible—it is unprecedented. Those are being deployed at speed and at pace. I also think that the Government is listening. I am absolutely convinced that, as circumstances emerge and as, visibly, we see those support packages that are working more or less better, Government will adapt to the circumstances as they are seen out there on the street.

Q170 **Rushanara Ali:** But the perception in our constituencies with regard to small businesses, with respect to what you are saying—I share your viewpoint about Government operating in unprecedented circumstances—is that big and medium-sized businesses are being looked after and small businesses are really struggling and not getting the help as quickly as possible, and that is where the urgency is required. That is what's happening. Are you feeding those messages directly to Government very firmly—very strongly? This Committee will do the same and we will keep doing it, but the important thing is acting quickly, because those businesses are not surviving. Some of them are not surviving and some of them won't survive, because of a failure to act fast enough to respond to them and put them higher up the agenda, which seems to be the case in every crisis.

Stephen Jones: What I would say is that we the industry are certainly feeling the pressure to do as much as we possibly can as fast as we possibly can and are working seven days a week, 24/7, to do what we can within the terms that have been made available. If Government chooses to change policy, and the bank part of the deployment mechanism and other, non-bank financial lenders that Stephen represents and the fintechs and peer-to-peer platforms do it, we will be delighted to support that effort as well and we will do everything we can to make it a success, but I can tell you that the Government, which we engage with on a day-to-day basis—

Q171 **Rushanara Ali:** I'm sorry to interrupt, Mr Jones, but would you recommend that the Government choose to make that decision? Should the Government make that choice? What would you say? I am very grateful for all that the banking sector is doing and all that you are doing seven days a week—everybody is working very hard. Should the Government be doing this?

Stephen Jones: That's a political judgment and I'm not paid to give political opinions here. I'm here to represent the banking industry and to make sure the banking industry does everything it possibly can. One of your fellow Committee members—the Chair, I believe—pointed to the moral hazard issues if you effectively give grants to all businesses and take the risk that you are giving them to businesses that would have failed anyway. I think there is a threshold, which we need to understand. We need to make judgments about what side of that threshold we want to be on. I want to see as many businesses as possible that have the chance of surviving this crisis being able to get through this awful downtime that we are all suffering, for the good of the economy and the good of our society, and I know that my members want that as well.

Q172 **Rushanara Ali:** How closely are you and others looking at moral hazard for big and medium-sized businesses? And can I ask you one final question—a supplementary? At the outset of the scheme, there were lots of reports of small businesses being offered loans at a very high rate—with the guarantee, of course, but that's gone. Is the high-rate practice still continuing? Do you have any evidence of that happening or has it been addressed?

Stephen Jones: Those high rates under CBILS are not loans that I recognise, because CBILS loans were 80% guaranteed by Government, so they should not have been offered at a high rate. The average unsecured rate, even before CBILS, in January was in single digit figures across the major lenders. There may be higher-risk businesses that were not eligible for CBILS that were being offered higher-risk financing, with a greater risk of the lender losing money, at much higher rates, but I don't recognise that characterisation of loans under CBILS being offered, even in double digits, and I wouldn't expect loans to be offered in double digits under CBILS. It should be mid-single digits—the kinds of rates that are being offered reflecting the guarantee and the risk profile and the security that is made available under those loans.

As for mid and larger loans, the Government is working on what it calls CLBILS for businesses with a turnover of above £45 million but with a sub-investment grade credit profile. These are the stranded middle who do not have access to the Bank of England commercial paper facility for the largest and highest creditworthy businesses. We are working very hard with Government on deploying that and making sure that it can get out of the door quickly. I see no difference between a small, medium-sized and large business in terms of whether one is more or less deserving than another of support in order to survive this crisis. They all play very, very important roles, both in our economy and in our wider society.

Chair: Thank you. I will go now to Anthony.

Q173 **Anthony Browne:** Thank you, Chairman. For the record, I should declare that I used to be chief executive of the British Bankers Association, the predecessor body to UK Finance.

Stephen Jones, you mentioned earlier that there were gaps in terms of support for businesses that weren't profitable at the end of 2019 or not seen to be profitable at the end of this. Are there any other gaps where businesses are not getting support? One group I am thinking of is start-up companies that clearly don't have a profitable track record and that might have had investment but can't get new investment.

Stephen Jones: I recognise that, Anthony. Obviously, many high-growth start-up companies have not yet reached profitability as they grow, deploy and develop their technology and business models. I think those businesses are absolutely critical to our economic future. Many of them are at the cutting edge of biotechnology and financial technology and are a really important part of why the UK is such a vibrant place to be from a technology perspective. They need equity. They can't sustain debt because they are not making profits, and you need to make profits in order to sustain debt. As you know very well, the banking sector cannot deploy equity. The regulator effectively has made that impossible—rightly, in my view. We therefore need to come together collectively to figure out where the equity will come from, if not from the founders of those businesses, to enable those high-growth but not yet profitable businesses to survive. That is clearly a policy question. I know policy makers are thinking about it, and a number of people in the private sector are thinking about it in working groups.

Equity will also be required for those businesses that do take debt on to survive the crisis but it turns out they do not have the financial strength as they come out of the crisis to support that debt. We will need equity in order to convert some of that debt into equity for those businesses as we come through the crisis. So there is an issue that we all need to think hard about in terms of finding a source of equity that enables us to support the businesses that you describe.

Q174 **Anthony Browne:** Are there any other groups of customers that fall through a gap? Either Stephen may answer.

Stephen Jones: Stephen Haddrill can talk about the non-bank financial sector. Many of his members and some of mine are in that sector. We are working on that. I have mentioned CLBILS. The Government hopes to deploy that in the next couple of weeks, certainly this month, for businesses with a turnover of above £45 million but below investment grade status. Investment grade companies have access to capital markets and the Bank of England commercial paper programme. Capital markets are slowly resuming for issuers in that space. I am probably missing something, but that strikes me as being the spectrum of businesses, from the small to the largest, and where the gaps are. I think CLBILS will largely bridge the gap between the existing CBILS programme and the commercial paper programme that is already out there, but we need to see the full details as that is deployed in order to be sure of that.

Anthony Browne: Stephen Haddrill, do you want to come in?

Stephen Haddrill: I do think that access to the CCFF for the non-bank sector would be extremely helpful to them. As I said before, I think that they themselves are struggling to raise money. The other point I would make is that so much of the focus at the moment and so much of the financial support is about forbearance—it is about just keeping businesses alive by deferring loans, deferring payments and so on. I feel we need to work out where we are going to be in three to six months' time. How will we get investment money into business and not just money to keep them alive? I think that could turn out to be quite a big gap if we do not think about it clearly beforehand.

Q175 **Anthony Browne:** Thank you. Stephen Jones, you mentioned—and Stephen Haddrill followed up with—the observation that the regulations are peacetime regulations, things like the due diligence that you need to do on KYC and other regulatory requirements. Are there any particular regulations that you think should be suspended now to help facilitate lending to small companies?

Stephen Jones: At the smaller end, I mentioned the three areas, and the Consumer Credit Act is the most difficult. It is a very arcane piece of 1974 legislation. The liability associated with getting your statements wrong—in the wrong format and at the wrong time to borrowers—means that the loan is completely unenforceable. So the risk-reward of taking a risk with the Consumer Credit Act and getting out there and making the loans that you want to make to businesses at the smaller end of the spectrum is pretty horrendous for firms in relation to that piece of legislation. But I recognise that, as we are operating in wartime, the opportunity to properly reflect on the Consumer Credit Act and change it, which is something that we have all talked about for many years, and doing that at haste in the current environment, might be difficult. But I would point to that particularly.

I think that the FCA, in terms of its own rules in the consumer credit space as they relate to smaller businesses, is showing flexibility, which I applaud, just as it has been showing flexibility around consumer forbearance in the unsecured space where it has suspended some of its CONC rules which would otherwise have made that forbearance difficult. I certainly think that we need to look at the Consumer Credit Act as soon as we can. It has all sorts of perverse consequences. It did not work in peacetime and it certainly does not work in wartime.

Q176 **Anthony Browne:** Thank you. I have one last question. I have had some complaints from constituents about bank branches being closed. I do not mean permanently closed, but closed during this crisis, presumably for staffing reasons. As a result, they have trouble getting loans out. What are banks doing to try to make sure that they can keep branches open so that businesses can go in there? Clearly, there are other routes in, but, obviously, people often want a face-to-face meeting.

Stephen Jones: Yes, I recognise that. On average, 75% of branches are open at the moment. The working hours have shortened in some places from 10 till 2, and about 90% of post office branches, which are also available to many SMEs, are open. Banks are doing everything they can to redeploy staff to those branches where footfall is greatest. Ironically, in town centres, which have been very empty as a result of people working from home, many of what were previously the busiest branches are now the quietest and staff are being deployed to more residential areas. It is possible that some businesses have been caught out by that, but banks are working hard to address that. Obviously, telephone channels, online channels and social media channels are also incredibly important ways of accessing information, speaking to advisers, to the extent that the branch is not available at a time that is convenient for the business in question.

Anthony Browne: Those are all of my questions. Thank you very much.

Chair: Harriett, I think you have a quick question and then I will go to Steve.

Q177 **Harriett Baldwin:** I have just one quick question for Stephen Jones. The burning platform out there in the economy is making payroll before the furlough scheme opens, and it does not even open until 20 April. Is it not something that there is, effectively, a 100% Government guarantee that they will get those payments for the furlough scheme? Why can your banks not be more proactive in lending against what they know they will get back from Government?

Stephen Jones: I think banks are doing everything they can within and outside the CBIL scheme. If it is clear that furlough is coming through on that date, I recognise that being able to lend against the certainty of that cash coming in is a relevant consideration, which, I hope, banks are taking into account. The CBIL scheme has its rules—and the rules are the rules—and the banks have to perform the credit checks according to the rules. Away from CBILS, I did mention that there is quite a lot of debt forgiveness—interest payment holidays. I am sure that the ability to lend short term, away from CBILS, to businesses that are sure of getting furloughed money in is something that banks will want to be undertaking. I am sure that they are undertaking it.

Q178 **Mr Baker:** We are going to see some very large sums of money moving to people, often desperate, looking to survive in this crisis. Many of us will remember GRG and other scandals that have taken place. Moral hazard has already come up. To what extent are you persuaded that the institutions making these loans have the right culture and, more importantly, the incentives today to ensure that the people actually handling these loans make the right decisions and do not put their own interests first?

Stephen Jones: It is a fair and valid question, Steve. I believe that there are no disincentives to doing the right thing on the frontline. I think the industry recognises that it has a unique opportunity to restore its reputation, particularly with the SME community, in the light of some of the scandals that you reference. What I see and what I hear on the frontline every day are a bunch of extremely motivated and very hard-working individuals who are incentivised and motivated to do the right thing and to be seen to be doing the right thing. I really, really hope that we will not see anything like the repetition of the previous history to which you referred.

Q179 **Mr Baker:** Thank you very much. Of course, we are all grateful to those people who are doing the right thing, but you referred earlier to the scale of the economic shock. I think we have to accept that it will be followed by a social and, potentially, a political shock. What I'm really driving at is: do you think the connection is there between the intent of senior management and the incentives and culture of the people much lower down in the organisation, to make sure that they appreciate the sheer scale of what is at stake with people's livelihoods, the social effects of the decisions that are taken, and the subsequent political effects? It is possible we will see a new normal after this crisis, and we want it to be a good one. Are the incentive structures adequate to ensure good conduct?

Stephen Jones: I believe that firm cultures, which is really what you are talking about, have fundamentally changed and that the connectivity between the top of the organisation and those on the frontline is much stronger than it has ever been. The values-based messages that were being delivered even before this crisis, but even more so during it, are strong and heartfelt and are being dispersed across the organisation in a way that enables frontline staff to do the right thing and to use their judgment in the appropriate way. But banks have to consider not just those customers whom they wish to help. They have to consider the wellbeing of their colleagues, the interests of their shareholders, and the rules that the regulator and the Government apply to them. They have to make sense of all those factors in attempting to do the right thing. Unfortunately, they aren't able to give money away and hope that they'll get it back. There has to be a structure within which that money is provided.

Q180 **Mr Baker:** I will make this my last attempt at extracting the answer I am looking for. That was all very reassuring stuff, but my fundamental point is about how people are remunerated. Are the mechanisms that will lead to people's bonuses at the end of the year suitable for ensuring we get the right conduct? It is really about remuneration, bonuses and making sure that, when people are taking a decision on behalf of a bank, they take the right decision overall for society.

Stephen Jones: You know very well how remuneration, particularly for senior staff—material risk takers, as they are called—has changed substantially, and that up to 70% is now deferred over multiple years, with the right to clawback if it turns out that the wrong thing has happened on a senior manager's watch. You also know that Sam Woods wrote to the big seven CEOs on 31 March, making it clear that he did not expect any cash bonuses to be being accrued through 2020 by any senior manager or any material risk taker.

I then wrote to Sam to clarify that that did not prevent cash bonuses from being deployed to frontline staff who are undertaking frontline work at relatively low pay levels and under acute pressure. He made it absolutely clear that this prohibition did not apply to frontline staff, who can and should have the ability to receive cash bonuses this year for doing the right thing. I hope the combination of forbearance at the top, and the ability to pay cash bonuses to the staff who are actually out there on the frontline, creates the right combination of incentives that you refer to.

Chair: I am going to come to Julie in a moment. Before I do that, I am aware that Stephen Haddrill has been included in the conversation a little bit less than the other Stephen. I will give you a minute or two after Julie has finished to share with us any thoughts or observations. There is no need to take up that offer, but I will let you come in after Julie.

Q181 **Julie Marson:** Thank you. You have alluded to it briefly, but I want to turn to the large business interruption scheme, which covers a hugely important sector of our business community, employing something like 30% of the private sector workforce. When do you expect lending to that sector to begin? You mentioned later in the month. Have you got anything more specific than that?

Stephen Jones: Lending to that sector continues. Actually, because it is a bigger sector and probably a bit more resilient than smaller businesses, existing funding is still available. Existing lines can be drawn on, and existing overdraft facilities can be used within the sector. Lending has continued irrespective of there not being Government support for now. My understanding is the Chancellor's intention is that the new scheme should be made available within the final 10 days of April, and that is the timetable that the industry is working to in order to deploy the new scheme.

Q182 **Julie Marson:** Do you think that, from day one, we have learned anything from the previous schemes that will enable lending under that scheme to be ramped up more quickly where it is needed?

Stephen Jones: Lending to bigger companies is inevitably more bespoke. I think the intention is that lending should be not necessarily all on an interest-free basis but should reflect the implicit risk—that there will be a Government element to guaranteeing some of the credit risk associated, making it easier for the banks to make loans of the size the businesses may require. The fact that we have had a couple of weeks to talk about it with Treasury officials and with the Government has given banks a little more time to prepare than they had previously. Inevitably, the original CBILS programme was delivered at very great speed and there was less time to prepare. I am hoping that the smaller volumes, the more bespoke nature of the CLBILS programme and the fact that we have a little more time to prepare will make it easier to deploy but, again, it is not all going to go out of the door on the first day. We need to be careful about the promises made in respect of the scheme.

Q183 **Julie Marson:** We do not know the exact terms in some respects. There have been some media reports that firms with a turnover up to £250 million might get loans of up to £25 million, and that those with a turnover above £250 million might get loans of up to £50 million. Is that your view?

Stephen Jones: I cannot comment on what the terms may or may not be, I am afraid, because they are not yet out there in the public domain and, actually, the Treasury, the Chancellor and the Government have not finally decided on what the terms will be. I have read that media commentary as well, and that seems like a reasonable assumption to work on.

Q184 **Julie Marson:** Do you think there are any particular barriers in the scheme for larger firms that will limit the scheme, limit demand or reflect the fact that more financing and loans are available to these companies in other ways?

Stephen Jones: It is hard to say without knowing what the final terms are going to be. Some lessons have been learned from CBILS, and the new scheme reflects very much the different needs and requirements of slightly larger businesses than the existing scheme that is out there. I very much hope that it will be as easy and as comprehensive to deploy by firms within the risk envelope that the Government define in setting up the scheme.

Q185 **Julie Marson:** Finally, to follow on from what Steve Baker said, do you think the banks will profit from the crisis in terms of extra interest, payment holidays and so on? If so, should they?

Stephen Jones: I think net-net, with the forbearance measures that are being taken, the extension of risk appetites to the absolute limit and the kind of economic contraction scenarios that the Office for Budget Responsibility is painting today, I find it very hard to believe that the banks will profit from this crisis. It is a question of how significant the losses will be. At the same time, I would point to the very fast action by regulators to release capital buffers and to make it clear that they are there to be used to support the economy at a time of crisis in order to ensure that the maximum amount of lending can be deployed by banks in the circumstances.

Julie Marson: Thank you very much.

Q186 **Chair:** Stephen Haddrill, do you wish to share any further thoughts with the Committee?

Stephen Haddrill: Just a couple, yes; thank you very much, Chairman.

First, over the last 10 years we have seen, in the re-emergence of the non-bank and the independent sector, a sector that the FCA itself regards as very innovative and that is lending to people who are close to it. It is very close to the customer. Whatever can be done to support it is really important.

Secondly, the supply of credit is so fundamental that it has to be speeded up, and the supply chain of credit has got to be shortened. At the moment you have Bank of England support going into the main banks, which might then pass it on to the non-banks, and they pass it on to their customers. Let us short-circuit that and get that Bank of England support or British Business Bank support directly to that sector.

The other area where speed can be compromised at the moment is, as Stephen said, because of the Consumer Credit Act. In its latest guidance, the FCA has found some workarounds that work in the current three-month period. They work in that period because the FCA can say that it will understand that the regulations will be worked around and so on. But as we move out of that three-month period where you have a standardised approach to helping the customer, and into a period where I suspect there will have to be a lot of discussion with customers about whether they can really afford another three months, firms may be at greater risk of being accused of making the wrong calls in the future, and if they have not strictly followed the Act, they will be exposed to compensation claims. I don't think the CCA thing has been dealt with for the entirety of the crisis; it has been dealt with for the next two to three months at most. Finally, I would say that we all need to put our thinking caps on about what happens after the three-month period and do so as quickly as possible.

Chair: Stephen, thank you very much indeed for that very helpful contribution. Thank you to both of you; that brings us to the end of this session. It has been particularly useful to have examined some of the hindrances, as perhaps we might term them, in getting the money out. That has given us food for thought and things to take up with Treasury and with the regulators who will be on the next panel. My one request is that you both write to the Committee about the information that you believe you can continue to provide on the level of applications that you are getting to your members for finance and the amount of finance that is actually being provided, and the frequency with which you may be able to provide that information. That would be extremely useful, because it would allow us as a Committee, the Government and others to carefully scrutinise exactly how we are doing in what is a very time-critical moment for the economy. Thank you very much indeed for joining us. That brings this panel to an end.

Examination of Witnesses

Witnesses: Sam Woods, Sarah Breeden and Christopher Woolard.

Q187 **Chair:** I believe we are now going to move seamlessly on to our second panel. Can I just confirm that we have Sam Woods, Sarah Breeden and Chris Woolard with us at the moment? We do. Yes, I can see Sam. Great. I will take it that you are all here, present and correct. Thank you very much for joining us. Perhaps we could just start with a brief introduction from each of you—starting with Sam Woods, if I may?

Sam Woods: I will be brief and just do three things very quickly, because I know Members want to get on to questions. First, our overall strategy is quite easily described: what we are trying to do, together with our colleagues at the FCA and the Treasury, is to build a bridge across the significant downturn that we are just at the beginning of now. The most important bit of that is probably what the Treasury is doing, through things such as the job retention scheme, the self-employment scheme and all the rest, but we have an important role as the prudential regulator to try to ensure that the financial sector can play its part in building that bridge. That is our strategy.

Secondly, what does that actually mean at a very high level for banks and insurance companies? On the banking side, I would pull out four things: first, we have cut capital requirements quite significantly for the banks, and in particular we have taken away the counter-cyclical buffer, which frees up £23 billion in capital. Secondly, we have been working with the banks to keep capital in the system, of which cutting dividend distributions is by far the most important aspect. Thirdly, we have put in place something that is launching today, the TFSME, which is up to £200 billion or so of cheap funding based on our previous experience of such schemes. Finally—this sounds less important, but it is probably just as important—we have given some guidance on accounting for IFRS 9 and the capital treatment provisions, in order to avoid those things unwinding everything that I have just described.

On the insurance side, it is a bit more of a mixed picture, because you have a far wider range of business models. We entered the crisis with reasonable levels of capital, and the insurers have largely weathered the first storm in terms of all the financial market movements, with a modest impact only on their capital coverage ratios and their liquidity. There are two main things that we have an eye to from the prudential side. One is on the general insurance side: the cost of claims, of course, which should and are coming through, and must be paid. Secondly, there is the possibility of liability stresses, if we conclude that those may accelerate further, in areas like business interruption and travel.

On the life insurance side, the main thing we are watching is the risk of default and downgrade in the corporate sector, which would have quite a big impact on both the capital and the coverage ratios of life insurance companies. That is rather more a case-by-case approach on the insurance side.

Thirdly, and briefly, we are doing one other thing: we are trying to take pressure off the system so that both we and the people in the banks and insurance companies can focus all our energies on fighting covid-19. There are two planks to that. One is supervision. We can go into the detail, but crudely you can think of it as us pushing out lots of things that we do not need to do right now in order to free up more space. The most visible thing we have done is cancel this year's stress test.

The other plank is on regulation. We are making a wide range of what you could think of as tweaks to ease the system through what we are going through. I could give you many examples, but in the interests of time I will give one—the international one. We argued at Basel that it would make sense to push back the reforms that we call Basel 3.1 for a year. That was agreed and is going ahead.

Q188 **Chair:** Thank you very much. Could we have brief introductions from Sarah and Chris, please, to check that you are with us more than anything else?

Sarah Breeden: Hi, you have got Sarah Breeden here. I am the executive director working for Sam, responsible for UK banks.

Christopher Woolard: I am Chris Woolard, the interim chief executive at the FCA. To add quickly to what Sam just said, clearly from our perspective the strategy and the bridge that Sam outlined is the same one that all the authorities are pursuing. For us, there are three things that really characterise what we have been up to. First, in respect of financial markets, we are trying to ensure that they remain open and orderly, and in particular that the very large firms, pension funds and others that rely on those markets can have the necessary adjustments to make sure that orderliness continues. We can come back to that.

The second, and probably biggest, piece we have done is around consumers, ensuring that we act to support the wider initiatives the Government is taking: for example, making sure that people keep a roof over their head if they have a mortgage. We have taken measures around consumer credit to ensure there is an element of breathing space there. Then, we are increasingly looking at other markets like insurance in the work we announced this morning.

In respect of firms, just as Sam said, we are easing a lot of the new regulatory work that would have otherwise been done. We want to make sure that firms have got the space to tackle this crisis in the best way we can. We are adjusting our rules and tweaking them where we need to. We are also working closely with certain groups of firms: for example, we are co-ordinating with banks and building societies around where they have their branches open and whether their call centres are open. We are keeping a close eye on those essential frontline services.

Finally, as you would expect, we are also planning for what the next phase of this might look like. We know there will be firms that will be in difficulty and there will be a greater need for things like debt advice for consumers. How do we begin to start to put those things in play as we walk forward in this crisis?

Q189 **Chair:** Chris, we heard in the last panel session about various of the banks' obstacles, as they are perceived, to getting money out and speeding up the process of getting loans through. I want to ask you about two specific points raised. First, I think Stephen Jones described the Consumer Credit Act as unfit for purpose in peacetime and certainly unfit for purpose in wartime. Do you agree with that? If so, in what respect, and can anything be done as a workaround of the problems there? Secondly, there was a desire from banks—perhaps you would expect this—to have 100% guaranteed coverage from the Government. What are your thoughts on that? Particularly as a regulator, what are your thoughts on the additional risks that would be introduced were the Government to do that? How might you monitor and try to accommodate those risks?

Christopher Woolard: On the first of those questions, it is worth saying that the provisions of the Consumer Credit Act are in primary legislation. It is quite unusual in the sense that so much of it is actually embedded in primary legislation. For small firms and the wider CBIL scheme, there were a couple of technical things in our rules that needed to be clarified. We have done that, and I think firms are very happy with what we have done, in terms of allowing banks to get on and lend, knowing that they have got the criteria right. That was done very early in the process.

In terms of where aspects of the Consumer Credit Act bite, they generally do not bite on larger firms—it is only the microbusinesses that they bite on—but they attract themselves to ordinary consumers and some of the packages we have put in place. For example, the Consumer Credit Act is relevant to the work we have done around credit cards, loans and overdrafts. At the moment we have a combination of individual firms that we are helping to work around some of those provisions, which are quite tight. Most firms found a way of giving the necessary paperwork to their customers or members, if they are a building society, which frankly is an inconvenience in the current climate. The current crisis shows that there are aspects of the Consumer Credit Act that you would change in time, but I am not sure that anything within it right now is stopping people getting on and either lending money or giving forbearance, but it does make things somewhat more complicated, I completely accept that.

You then come to the question of the Government's loan scheme towards CBILs and other businesses. Clearly, the risk levels within that—the moral hazard question, which has already been mentioned in the previous evidence session—are a matter for the Government to think about, not us, as the regulator. However, I can say that there are clearly trade-offs here between the speed with which money is flowing towards small businesses and the ability to repay. As Mr Baker mentioned in the previous evidence session, we run into some issues from the past around what happens when you have firms at the end of this that are potentially in distress and how to treat them. That is one space where we are paying close attention.

What is different from last time is that we now have the senior managers regime in place, which allows us to look across into unregulated businesses being carried on by banks and others. This morning, we actually published a letter to banks around how we expect them to conduct themselves towards small firms in this situation, what we expect from their boards, in terms of oversight, and the fact that, for the first time, we are setting up a small business unit within the FCA that will look statistically at these questions as we move through the crisis.

Q190 **Chair:** Thank you. Just to take the banks' corner for a minute, we are saying to the banks that the Government will guarantee 80% of a loan as it is at the point of default, but at the same time we are going to require them to judge the viability of the business on its performance prior to the CV crisis emerging. We are also going to restrict their ability to have personal guarantees, particularly at the lower level of these loans. To take an unconventional view of this, perhaps, are there any concerns that some of these banks are being put in quite a difficult position? That might be fine for some of the larger ones—I do not know— but for others that are being constantly pushed to get the finance out there, are any of them taking undue risks overall or being pushed into that situation?

Christopher Woolard: I don't think we see a position at the moment where there is undue risk, but Sam and I are jointly collecting information from banks about what is happening with this, in terms of what business is actually being written, the level of risk being taken and the terms on which these loans are being given. We are building that picture right now.

It is true and fair to say about the situation that banks find themselves in that they have historically had quite small teams that specialised in business lending but now have very high volumes of demand coming towards them, and they are having to respond at speed, at a time when they do not necessarily have all their staff available to them and in full health to work through that demand backlog. So there are issues and pressures that have built up here, but what we are not seeing at the moment necessarily is a different risk profile being built up

Q191 **Chair:** Thank you. I have a final question, and I ask anyone who wants to come in on this to do so. If the Government were to move to 100% guarantees, do you think that would be a complete game-changer? Would that turn what most perceive to be a bit of a trickle, albeit that there has been an uptick more recently in getting the money out, into a quantum increase in the amount of money that is getting to those businesses that deserve it and need it as quickly as possible?

Christopher Woolard: Clearly, again, that is a matter for the Government, but where we see schemes, for example, the Swiss scheme, whose terms are very different and the guarantees given in the scheme are very different, clearly they are a very efficient transmission mechanism from central Government, through the banks, to small firms at speed. But there are then questions such as, "Okay, that's fine for now, but what happens when that money needs to be repaid?" So they come with a different balance of risks that would need to be considered. But, as I say, those are squarely questions for the Government to consider, not for us, as the regulator.

Q192 **Chair:** But what I am really asking is not so much whether there is a policy position that would be the right one—that is indeed for Government to decide—but whether the banks would, in that eventuality of a 100% guarantee available, kick-start a hugely increased flow of lending.

Christopher Woolard: If you look at the two schemes where the flow of lending has been very fast, those in Germany and Switzerland, what you have attached to them is not just a 100% guarantee, but some quite different terms, for example, as to what proof has to be given by the firm of the need to fund it. If you were to adopt those, it is a reasonable factual assumption to say that those flows would be quicker, but, as I said, they will come with a different set of risks attached to them that would need to be thought about in the round.

Chair: Okay, thank you, Chris. I am going to go to Anthony now.

Q193 **Anthony Browne:** Thank you, Chairman. I have questions about the support for businesses in particular, rather than retail consumers. This is a question for the FCA and then there is one for the PRA—they are separate questions. On the conduct side, Chris, are you looking at the terms being offered by banks to businesses taking up CBILS? Do you have any particular concerns about the terms of those lending?

Christopher Woolard: We are collecting data on that at the moment, so we do not have a reliable picture of what those terms are right now, but we will within a few days. Sam might like to say a little more about that in a moment. We are certainly looking to see what is going on. In terms of establishing a team within the FCA purely concentrating on small businesses and the terms of what is going on between banks and them, we have two real main objectives here. The first is, in what is an unprecedented situation, as everyone has already said, helping the banks through it in terms of making sure they are doing the right thing. But then we also need to make sure we are paying close attention to both the terms of what is going on there and the longer-term treatment of those small businesses that need help, and ensuring that boards of banks and building societies are also discharging their responsibilities properly in terms of keeping the oversight of that function within their firms.

Q194 **Anthony Browne:** One issue that has been the subject of comment in the media is the interest rates after the one-year interest-free period. Are you satisfied that they are fair and reasonable, and actually represent the risks the banks are taking on?

Christopher Woolard: Again, we are gathering information on that at the moment. What we do not have is a picture across the market of exactly what is happening there. Clearly, in the first instance it is going to be for banks and their boards to make a judgment on the fact that they are treating those customers fairly.

Q195 **Anthony Browne:** Okay, a potential question for Sam Woods or indeed Sarah Breeden. Do you have any particular concerns about the risks of these loans and whether the banks are properly assessing the riskiness of those loans? Do you think the banks are justified in asking for personal guarantees for the higher-value loans of over £250,000?

Sam Woods: I will begin and then Sarah may wish to come in, too. I am not currently concerned about that. The capital treatment for these loans is strong enough to cover the losses that should arise in the normal way from making loans of this kind. The overwhelming issue that we have been hearing from the banks about the blockages is that they are kind of operational blockages and bottlenecks. Between the Government and the banks, they have been trying to work through those. One that has not been mentioned yet, which I think may be relevant, is that because the scheme has its origins in the British Business Bank, some of the banks are using their enterprise finance guarantee systems, which are a BBB product, as you know. If we can get it out of that channel and into the mainstream systems that they have, which might involve the British Business Bank taking more of a portfolio approach, rather than loan by loan, that could free up things further without adding any additional prudential risk. I know that that is under discussion with the BBB at the moment.

Q196 **Anthony Browne:** Sarah, do you want to add anything?

Sarah Breeden: The only thing I would add is that I very much agree with Sam that in our discussions with banks to date and in what we have seen of their credit risk assessment processes, there has been no suggestion yet that banks are taking undue risks through these decisions. The eligibility criteria are very clear—the business has to be viable as at December '19. That is not the usual way that firms are assessed, particularly at the smaller end of this spectrum—the credit risk associated with these firms—but they have done a good, if manually intensive, job of trying to ensure that the risk assessment and the eligibility judgments are made in line with the scheme. So it is not a concern at present.

Q197 **Anthony Browne:** Can I push the point on personal guarantees? Clearly, when the scheme was initially launched, there was a lot of concern and complaints from businesses that they had to make personal guarantees for loans that were 80% guaranteed by the Government. The Government changed the rules: that now only applies to loans over £250,000. Do you think the banks are justified in asking for personal guarantees for loans that are 80% backed by the Government in any case? Is that not belts and braces from a risk appetite point of view? I'll ask Sam that first and then Chris might want to come in.

Sam Woods: It is a risk appetite choice between the Government and the lenders. Our job is just to capitalise what is left in terms of a residual risk, if you like. We can do it either way. Obviously, if you look over on the consumer side, it is perfectly normal to have houses as collateral for mortgage-type contracts. That is one of the reasons why capital requirements for mortgages in this country are so low. I think you can do it either way, but I do not think it is a strange or unusual thing for the banks to be looking for for those bigger loans. But I do think it is very helpful for that lower level, which is still quite significant, that it has been taken away.

Anthony Browne: Chris?

Christopher Woolard: To add to what Sam says, it is a question between the banks and the Government, in terms of the banks—that arrangement that they are making.

Q198 **Anthony Browne:** Okay. You responded very well to that interruption behind you, Chris. It wasn't a child coming in—oh, maybe they are coming in again.

My last question is about start-ups. You were in on the last session when I asked this question of the banks—that there is a hole for support for start-ups. Clearly, they are normally not profitable. They do not have the normal track records for banks to assess whether they are or are not viable. They need equity rather than loans. The FCA has been very supportive of the whole fintech sector and start-ups there. You have a statutory duty to promote competition. Do you have any particular concerns about the impact of this crisis on start-ups in the UK, and is there anything that you think could be done to help them?

Christopher Woolard: There are a couple of things. It is not just the start-up layer, but the wider non-bank lenders layer that we talked about in the previous session. Both of those are going to need a level of support to come through the current disruption. I know that the Treasury and others are thinking about this very closely. We then put in to that, particularly around the fintech sector, but it is in the next stage of things that we know that the Treasury are looking to consider it.

Anthony Browne: Okay. My time is up. Thank you.

Chair: Thank you, Anthony. Alison Thewliss.

Q199 **Alison Thewliss:** I wanted to pick up a little bit on some of the things that Steve Baker had asked before, around the potential for a GRG-type situation emerging. The Select Committee has previously expressed concerns that commercial lending to SMEs is outside the regulatory perimeter. So I was going to ask—perhaps Mr Woolard, first—how will you ensure that SMEs are adequately protected from this type of behaviour this time around?

Christopher Woolard: The sound wasn't brilliant there for a second, so forgive me if I have got this not quite right, but I will have a go. I think the question was around small businesses being outside the regulatory perimeter. In broad terms very little business lending is regulated directly by the FCA—so just the micro-businesses, generally when it is a sole trader: the FCA has a degree of regulatory oversight of that, as if they were a normal consumer. For business lending, it sits outside of the regulatory perimeter. However, what we have since the last financial crisis is the introduction of the senior managers regime. What the senior managers regime allows us to do is to look at the individual who has been appointed within a regulated firm to have oversight of that unregulated business and to consider the conduct of that individual and indeed of the board towards oversight of that individual. What we have done this morning is actually write to all the major banks that are participating in lending to small businesses and saying to them, during this time—obviously we are being supportive, wherever we can be, in terms of, for example, the CONC rules that would need to be tweaked, or given an opinion around, to allow some of this lending to occur; but we also expect boards to be having strong oversight of those who engage in small firm lending. As I said, we have set up for the first time a new small businesses unit within the FCA that is specifically looking at this kind of conduct going forward.

Q200 **Alison Thewliss:** Can I ask about those units, and how small firms will be able to access that, perhaps to raise concerns? Will that unit look outwards as well, and make sure that small firms do not end up in a GRG-type situation?

Christopher Woolard: I think there are two main sources of protection for small firms in this. The first is for 97% of small firms—so those, generally speaking, under about £6.5 million turnover, or less than 50 employees. They can actually access the financial ombudsman. We changed the rules last year, in 2019, to give them access to the financial ombudsman with any particular complaints they have about their own treatment. The second part of this is, as I say, we have got this unit established now. Small firms can contact us direct through all our normal channels. Our call centre is operating normally. Our website is operating normally. I think if a firm has got a concern it should get in touch, but in the first instance if it has a complaint the procedure is they should complain to their own bank or building society and they can then take that issue to the ombudsman if they are not satisfied—and then *[inaudible]*—which, as I said, 97% of small firms are.

Q201 **Alison Thewliss:** Lenders are clearly going to make a call on the viability of businesses. How can you make sure, in this fast-moving situation, that they do that properly?

Christopher Woolard: Yes, this is clearly a very difficult judgment for individual banks to make. They are clearly being asked, within the rules of the CBIL scheme in particular, to take a view of the viability of a firm based on its past performance, rather than its future projections, which is quite an unusual situation to be in; but I think it is one of the key adaptations that financial services firms need to make at this time. We will support firms through making those kinds of judgments by tweaking our rules when we need to, but ultimately I think the thrust of what the Government has put in place, and the way banks are approaching this—it is about supporting viable firms through the crisis. It is not about propping up firms that were failing in the first instance, and that, obviously, is a judgment that needs to be made case by case, and a series of individual lending decisions.

Q202 **Alison Thewliss:** Do you think there are particular sectors where businesses might find it more difficult to prove that their business is not failing but is viable?

Christopher Woolard: Some sectors are perhaps slightly harder hit than others by what is going on, but we should remember that the OBR figures published yesterday show that this is a very significant economic shot across the bow of the whole economy. I do not think that at the moment we are seeing a picture of particular sectors struggling, but Sam and I are building that picture in terms of the lending data we want to see.

Q203 **Alison Thewliss:** Finally, are there any other sectors outwith the regulatory perimeter that you think might be problematic in this situation, and is there anything else we need to be looking for?

Christopher Woolard: I think I heard the question correctly. We are seeing a picture around scams linked to covid-19 where there are industries, if we can describe them as that—or rather, often criminal activities that are operating well outside the regulatory perimeter but are trying to mimic things that are regulated activities. Clearly, we are taking action on those; we have issued more warning notices than at pretty much any time in the last few weeks. In any crisis there will always be people trying to take advantage through scams.

Alison Thewliss: Thank you.

Chair: Thank you, Alison. May I turn to Steve now?

Q204 **Mr Steve Baker:** May I begin by thanking you and all your staff for what you are doing, and pay particular thanks to Chris Woolard, because he has stepped into one of the trickiest jobs in public policy? Thank you very much indeed for doing that.

I want to turn to the covid corporate finance facility and ask Sam Woods about the Bank's capacity to operate the facility. Does the Bank have the capacity, and from where has the Bank found the people to staff up that facility?

Sam Woods: Mr Baker, thank you; your comments will be much appreciated by all our staff, and I am sure Chris's as well.

Yes, we have got the staff to operate that facility. Our latest published number in terms of the drawdown was for last week, when it stood at £5.5 billion, and the very latest number I have, from my brief, is £7.6 billion, so that is going at a pretty decent clip. It is of course by volume of companies a much smaller, and therefore more operable, scheme than CBILS. To give a sense of that, we have had 237 applications so far, of which 51 were ineligible and the rest are in various stages. We have however had to raid, if you like, various areas of the Bank in order to provide that infrastructure, and the work is being led by Sarah's colleague Alex Brazier, and some of his financial stability team are on it too. Sarah and other executive directors around the Bank have been willingly pitching people in, and that has been manageable so far.

It is also the case of course that the banks can help people who want to join the scheme get ready and do the documentation and other stuff, so we have leveraged ourselves a bit through the banks as well.

Q205 **Mr Baker:** You are talking about serious money here of course; it trips off the tongue, but this is £7 billion of commercial paper bought. Are you completely convinced that all the staff involved have the necessary expertise to manage the risks involved in such large sums, fantastic though it is that they have all pitched in to operate the scheme?

Sam Woods: I think so. Inevitably, the Treasury as underwriter of this scheme is running some credit risk in doing this. Of course, it is drawn at investment grade, but I think we have enough; we of course have our own credit risk experts who are playing into the process.

I would mention that a very early problem we hit was that of course some large companies who are of very good credit quality do not have a rating because they have not needed to go to the markets, and there we have found a way to use commercial banks' internal ratings to achieve the ratings for those firms. So there we are, I suppose, outsourcing a bit of that judgment to the commercial banks, and how good we are in doing this job will depend a bit on how good they are at making those sorts of judgments.

Q206 **Mr Baker:** On that point about imputing ratings, there is also the issue that some firms will perhaps not be accustomed to issuing commercial paper. What is going on in the margins where those two factors—the combination of imputed ratings and perhaps not previously issuing commercial paper—come together? Are those firms going to get the money they need, and how?

Sam Woods: They will, but you are on exactly the right point, because that is where the commercial banks need to help. In effect, the commercial banks are—I do not know if "marketing" is quite the right word—going to companies and saying, "Are you aware of this facility? If you don't already have a CP programme with us, we can create one for you and we can then put it into this facility." That is the way that is happening. I feel pretty optimistic about that scheme. Some of the coverage has suggested that the numbers ought to be going up quicker than they are, but I think it is going reasonably well in terms of volume.

Q207 **Mr Baker:** These are large sums of money. It is a demand-led facility, as we have read elsewhere. It is financed by central Bank reserves. What are the prudential implications of operating the scheme, if any? To what extent have you considered what it means prudentially for the whole market?

Sam Woods: If you look at it narrowly from the prudential regulator's point of view—Sarah may want to come in as well—this is effectively part of the strain that would otherwise fall on banking system balance sheets directly that is falling back on the state. You can take a view on whether that is good or bad—I personally think it is good—but narrowly, from a prudential regulator's point of view, it makes the degree of risk we are running in the banking system smaller than it would otherwise be. Ms Breeden might want to come in to give you a flavour of the revolving credit facilities and what has been happening there, because that is quite an interesting thing going on alongside the CCFF.

Q208 **Mr Baker:** Thank you very much. In the interest of time, can you tell us a bit more about the stranded middle? Obviously, we now have the coronavirus large business interruption loan scheme, but is there more that needs to be done to straddle the gap between those interruption loan schemes and the coronavirus financing facility?

Sam Woods: The most important bit is the CLBILS, which the Government are about to bring out and that you were talking about in the previous session. By bridging the £45 million to £500 million turnover bracket, that ought, on my estimation, to cover a significant portion of what had previously been missing. When we look at all the schemes together, we think they probably cover something like 80% of turnover and employment in the relevant sectors, which seems to be quite good. It would be hard to ever get to a complete and total coverage.

It will also be the case, to echo the point made in an earlier session, that for some firms, getting a loan will not be the right answer. They will not want to take on a loan or they will not feel it is right to do so, because actually the burden of that debt is higher. They will want to fall back on the job retention scheme or the self-employment income support scheme. You will always have a portion, perhaps quite a significant one, for whom it makes more sense to rely on those things.

Mr Baker: Thank you very much. I will draw stumps there so we can go on to other colleagues.

Q209 **Felicity Buchan:** First, I thank you for all the work that you are doing during these difficult and unprecedented times. I know that you are putting an awful lot of effort into it. My questions are on the solvency of the banking sector, so I will address those to the PRA. What do you think the main risks are for the solvency of the banking sector?

Sam Woods: That is obviously an absolutely key question for us. The biggest risk stems from the biggest uncertainty that we all face in terms of the economy, which is, what is the extent and nature of the drawdown on bank lending that will be needed to bridge the economy through this situation? We can all have a go at that, but of course none of us knows what the answer to that question is going to be.

Chris mentioned earlier the OBR scenario, which is perhaps worth bringing in, if you do not mind me extending my answer a bit, because it is interesting. It is only a scenario, of course, but their scenario is a three-month lockdown and, as I understand it, a three-month gradual lifting of the lockdown. They thought that would turn into a 35% dip in GDP in Q2, 13% for the year as a whole, but then a bounceback of plus 18% next year.

I think that is quite an interesting thing to look at, because we normally capitalise the banking system through our regular stress test, and the level of GDP drawdown in that stress test is lower than those numbers. The UK drawdown is 4.7%—quite an extreme recession by historical standards. But if you look at the unemployment rate, ours goes up to 9.2%; the OBR’s, I think, was around 10%. It is the combination of unemployment and asset price declines that really hits banks’ capital. So it is not at all obvious to me that the scenario they have described is worse. It is obviously very different, but it is not at all obvious to me that it is worse, and we are working through that.

The thing is that we are going into this with a well-capitalised banking sector. There is of course some limit at which you get beyond what we have provided for, and I think if you had a multi-year total shutdown of the economy, evidently that is outside what we capitalise the system for. We are doing work to try to work out where you hit that point, but my guess is that it is quite a long way out.

Q210 **Felicity Buchan:** I represent a constituency in central London, Kensington, where a lot of major businesses are headquartered. What I am hearing anecdotally is that a few of these businesses have extreme cash-flow issues in the short term. First, are you concerned about the level of defaults that we could see imminently? Secondly, do you think the banking sector is in a position to make new lending, if we have gone through major defaults, as we look to come out into the recovery phase?

Sam Woods: The prospect of corporate defaults is a worrying one for us, both on the banking side and on the insurance side, which we may come on to. The pattern so far, and I might invite in Ms Breeden to give a bit of flavour on this, has been of what you could call a stockpiling of liquidity by some of the larger corporates, who are drawing down on their revolving credit facilities. I will bring in Ms Breeden for a moment and then add one more point, if I may.

Sarah Breeden: What we have seen from the banks is that there have been very large precautionary drawdowns by the largest companies of what are called revolving credit facilities. We have seen drawdowns of tens of billions of pounds on those, and those amounts have then been put on deposit with the banks; they have not yet been spent. As Sam said, you might think of it as the corporates hoarding cash ready for an imminent shock. So I think that, in the near term for the largest companies, that risk of default does not feel very immediate.

There may be some who are not eligible for the CCFF scheme that we were discussing earlier in the session, perhaps because they were not of the required credit quality. Of course, as we see the further work by the Treasury and the Bank on the missing middle, hopefully we will be able to fill that. But certainly the intelligence that we get is that the banks have lent the money to the largest companies who have it on deposit, ready for when the shock hits—and the shock has not yet hit in scale.

Felicity Buchan: Sam, you had a follow-up point.

Sam Woods: I want to make one more point, if I may, which is about the capacity of the banks to lend. Our view is they have ample capacity from a capital point of view. Just to illustrate it with two numbers, if I may, I mentioned earlier that we removed this other capital requirement that is called a counter-cyclical buffer, and that had the effect, compared with where that requirement would have been by the end of this year, of putting £23 billion of capital back into the hands of the banks.

To put that in context, if you make an assumption about a target capital ratio and a risk weighting, that should support about £190 billion of lending to corporates and SMEs in stressed conditions. That £190 billion compares with a net lending to corporates and SMEs last year of £16 billion. I just give you those figures to illustrate that they have got the capacity.

Now, it can be true both that they have that capacity and are willing to use it, and also that there is a point of distress at which that runs out. That is true, and the question is: where will we land between those two points?

Q211 **Felicity Buchan:** As for individual consumers, are you hearing from the banks that many are asking for holidays on mortgage payments or consumer credit agreements? Is that something that you are hearing anecdotally?

Sam Woods: Yes, we are hearing a lot of that, and Chris might want to come in on that point. I will invite Sarah to explain for a moment something that we have done on the accounting side to make sure banks can give them those payment holidays without taking a huge hit.

Sarah Breeden: One of the things that the IFRS 9 accounting standard does is to make banks make a reasonable forward-looking assumption on the losses they might take. Ordinarily, asking for a payment holiday might be a reasonable indication of a customer being in financial difficulty, and therefore that a provision for a future loan loss ought to be made. We were concerned that that would deter individuals from asking for holidays and deter banks from granting those holidays. So we have sought to intervene, to make it clear that in the current covid crisis that is not necessarily an indicator of a future loan loss reserve.

What that means—I think Stephen mentioned this in the earlier session—is that 1.2 million individuals have asked for mortgage holidays, and that amounts to about 15% of all mortgagees. So we have seen a good response there.

Q212 **Felicity Buchan:** Great. I have one final quick question: are you in touch with your international equivalents, and how do you think our banking sector is coping in terms of solvency compared with banks elsewhere?

Sam Woods: We are very much in touch. Interestingly, in the European setting, of course, we recently left the main banking body within Europe as part of the Brexit implementation period, and covid-19 has rather cut through that. We have now become more involved than previously, because of these shared issues.

So we are in very close touch, particularly with the ECB and the Federal Reserve, and I would say that we are all facing pretty much the same range of issues. I think our banking sector goes in as well prepared as any others.

Felicity Buchan: Thank you.

Chair: Thank you very much, Felicity. Can we go to Rushanara, please?

Q213 **Rushanara Ali:** Good afternoon. Can I echo what other colleagues have said by thanking you for all the work that your organisations are doing?

I want to pick up on the issue around customer care and treating customers fairly. I will start with the fact that the £500 interest-free overdraft, and that package, is obviously very welcome. It is for three months. Mr Woolard, perhaps you could kick off by addressing a few points. At the end of that period, will compound interest be charged? How will you ensure that it does not affect credit ratings, because obviously that would make people worse off? And are you confident that the repayment arrangements in the future will not get people into difficulty further down the line?

Chair: Have we lost Chris? Chris, you are not coming through. Are you muted on your computer, by any chance?

Mr Baker: I think he has dropped off the call; the video has frozen.

Chair: Shall we pass that question over to Sam or Sarah while we try to find Chris?

Sam Woods: Sure. We have to defer to Chris on the roll-up question, but I think your question goes to the heart of treating customers fairly from the point of view of both individual borrowers and SME borrowers. The one point I would make from the prudential end is that of course there are the points around the senior managers regime and whether cultures have changed within banks, but it is also strongly in the minds of people running banks that by the time we are through all the misconduct that was unearthed by the last crisis, it is probably going to have cost the banks about £100 billion here in the UK. That concern and worry about making a mis-step may slow things down a bit, but it ought to reduce the risk of a further wave of misconduct on the scale we saw in the last crisis.

Q214 **Rushanara Ali:** So we shouldn't expect, in terms of implementation and making sure that compound interests are not charged, to see things done in a sneaky way? One of the problems, as you know—we have raised it in the Committee in the past—is that things have crept up later and agencies have had to respond after the event. There is also the issue around credit ratings; people will be quite anxious about that. In addition—we will come back to Chris when we can get him back on—payday loans and "buy now, pay later" loans are not included in the package. Do you have a view on that?

Sam Woods: On the former point, it would be very unwise for somebody in my position to offer you a 100% guarantee that everything is going to be done perfectly by all the banks in this. It is inevitable that a few things will go wrong, but I am cautiously optimistic that they are approaching it in the right spirit. I genuinely believe that is the case. Remember, the people making these judgments down on the frontline are experiencing covid-19 like the rest of us, and I think they are quite well motivated to do the right thing. On top of that, that shadow of the huge costs of previous misconduct will probably mean that the controls are a bit better and that both the incentive and the likelihood of doing things wrong are lower than before.

On the exclusion of payday loans, I do not have a strong prior on that. What I do know is that some of those lenders that are just outside the margins of the banking system that we oversee from a prudential point of view are experiencing considerable strain, partly because their normal sources of funding themselves have dried up somewhat. It may be that a decision to leave them out was also predicated on a view of what was necessary to help that industry keep running, but I confess that I am speculating a bit there.

Q215 **Rushanara Ali:** As you know, I have raised a number of times in this Committee the issues with mortgage prisoners. The affordability test switched to a relative test thanks to the work of the previous head of the FCA and others, and the team, but I wonder whether anyone can clarify whether mortgage prisoners will also be allowed to take the three-month payment holiday. Obviously, they were in a difficult position in the first place, there are over 100,000 of them, and covid-19 is going to affect them just like the rest of us.

Sam Woods: I confess that my very strong assumption is yes, but perhaps I could confer with Chris after the session and, if Chris has a different view on that or knows something I do not, get him to write in and respond to that point.

Rushanara Ali: Thank you. Do we have Chris back, perchance?

Chair: No, I don’t think we do at this stage, unfortunately, but we are working on it.

Rushanara Ali: Okay, well, I will just keep going and see whether others can answer.

Sam Woods: I will do my best.

Q216 **Rushanara Ali:** Thank you so much, Sam. In terms of your overall assessment—I know it has been a short period of time—do you feel that the treatment of customers by financial firms has been satisfactory since the outbreak of coronavirus?

Sam Woods: I think so far it has been okay, but in many ways the rubber has not really hit the road yet; it is only just starting to happen. One piece of evidence Sarah mentioned that is useful is payment holidays. They have been granted. The accounting has been handled sensibly. As far as I can work out that has all been done in a way that is perfectly sensible and fair. It of course involves a degree of risk for everybody—for the banks from a prudential point of view and for customers from their own finances point of view—but that seems sensible. But on the next wave of things to come, particularly the CBILS and how that plays out—and several members of the Committee have mentioned GRG, and nobody wants to see another GRG. Will that work out or not? I think we will have a much better feel in about a month or two's time.

Q217 **Rushanara Ali:** This is perhaps for both of you. Where do you see the emerging challenges? To some extent I suppose I am asking you to anticipate where those emerging challenges are. Certainly, from our caseload as Members of Parliament, we can see some of those signs. We are pleased where the Government are responding to some of the feedback, but some people would say that it will be vulnerable consumers and customers who could still be hurt, despite these programmes. For instance, access to banks and post offices and so on is going to be even more challenging for them. In some areas, the services are not going to be available. Can you see areas already that you are concerned about? Leaving aside the Government for the moment, how well placed do you think the system is now to be able to respond quickly to correct them, whether it is the FCA or others, in a way that it did not do—that it failed to do—with GRG and other scandals?

Sam Woods: I think I would point to two challenges; I'm afraid they are both rather obvious, but they may still be right. The first is the one you mention—of course customers who are already vulnerable will, in many cases, have their problems exacerbated by what is going on. That is likely to be an area in which the Committee may well want to continue taking a close interest.

The other one is more novel. None of us yet know how well this bridge is going to work and whether it will succeed in bridging very large numbers of companies—large, small and medium-sized—through this downturn. We hope that it will, but it is of course possible that it doesn't. If it doesn't, looking at it from a prudential end, that is potentially a pretty big deal, in terms of both the impact on the banks and the impact on the insurance side. That is the one that is a more unique and unusual circumstance, because of the very significant speed and severity with which this issue has arrived compared with what we normally experience in a recession.

Rushanara Ali: Do we have Chris back? Are we not going to get him back?

Chair: No. I think it is probably time to move on. Is Chris with us? No, he's not back yet.

Q218 **Ms Eagle:** I had some questions for Chris as well, but while you are scrambling to try to get him back, I will first ask Sam and the Prudential Regulation Authority about the OBR report, which came out yesterday. It contained pretty shocking figures on the size of the slowdown that is being caused, for obvious reasons of health, with potentially a 35% fall in economic activity on a quarter, which would be the largest annual fall—of about -6.5%, if the IMF is to be believed—that we have seen in the UK in 300 years. In those circumstances—the rapidity and the size of the exogenous shock that the economy is having—how can you shore up the bridge that you are attempting to build with your policies and your access to capital and trying to keep the financial system working? How can you shore that up and make sure that it is not actually creating even more danger?

Sam Woods: That is the central question for us on the prudential side and, indeed, I would say for the Bank as a whole.

The first thing I would say is that the OBR put this forward as one scenario and there is a lot of uncertainty, but what they have put forward is not implausible. Obviously, they are very well-informed. Also, if you just look around yourself and ask yourself, "Is it plausible that that portion of the economy has been shutting down?", I think probably most of us would give the answer, "Yes." But I would say that there are two caveats. One is the point I made earlier—that is, that the OBR also forecast a very sharp bounceback of 18% GDP growth in 2021. I have not looked back to see when we last had 18%, but my guess is that it has never occurred. Maybe it occurred after a war or before a war, or something like that.

Ms Eagle: Possibly the industrial revolution.

Sam Woods: Maybe the industrial revolution, exactly. It is unusual in the sense that you have this very alarming drop, but you also have a very unusual rebound in the other direction.

The other point that I would make is that when most of us hear a GDP drop number, you are calibrating it off recessions in the past. As I said, our own stress test, which is pretty severe, has a GDP contraction of 4.7%. But this is very different in the sense of what may happen to unemployment. The unemployment figures across the OBR forecast and our stress tests are actually reasonably close. You also have this huge support package from the state, which is part of what leads to the quite significant change in the fiscal position that the OBR described. That, looked at from the position of a prudential regulator, reduces the hit on the system. I think you need to factor all that in and not be overly swayed by that initial big drop, but it is a huge drop and it is very uncertain.

Q219 **Ms Eagle:** Earlier you were talking about potential corporate defaults, and saying that you were keeping a close eye on all that. Obviously, given the sudden stop to economic activity and that exogenous shock, there are large companies in certain sectors—one thinks of aviation and hospitality—that will take particular hits and may have to be given support. In those circumstances, rather than loading them with too much debt, do you think that it may be more prudent to take stakes in some of these sectors, so that when the economy returns, they can safely return to the market with Government support, rather than returning heavily indebted?

Sam Woods: Two comments on that. One is that I think that the choice of whether or not to do that is for the Government, not for us. My second comment is that your observation is correct in the sense that for some businesses—either ones that are so fundamentally impacted by covid-19, or ones that were in not a very strong state to begin with—the answer is not to load them up with more debt. Equity funding may have to be the answer for some of those companies. Now, that can come from a lot of places; one major high street retailer actually raised equity within the last couple of weeks at a not unreasonable price. It may be that a market solution is possible. If it is not, I guess there is a choice for the Government, and it is a difficult one.

Q220 **Ms Eagle:** Thank you. I understand that Chris is back. I want to ask you, Chris—from the FCA's point of view—about how you are proposing to protect vulnerable customers, and I wanted to ask you a little bit about the pensions market in this instance. Two weeks ago, you published a press release jointly with the Pensions Regulator, and the Money and Pensions Service, calling on savers to stay calm and not rush into financial decisions. Could you tell us a bit more about how you would prefer pension savers to be responding at the moment?

Christopher Woolard: Thank you very much. May I just apologise to the whole Committee for having a bit of a technological meltdown at my end?

Ms Eagle: We've all been there.

Christopher Woolard: In terms of pensions in particular, the group that we are most worried about is the group of pensioners who are the first to have had the Government's pension freedoms and options available to them. They may not be invested in a long-term vehicle; they may be in some sort of drawdown vehicle, for example. Therefore, it is very alarming when you see the price drops that you see in financial markets in wider funds. As an investor, you'd think, "Right, I've got to sell now." We very much want pensioners—particularly those who are sitting there with large pension pots—to keep a cool head right now. We will undoubtedly, if history is any guide, see a degree of recovery in markets over time. If people do feel that there is a real pressure on them for some financial reason to sell a very large number of investments right now, what we have said is: go and seek financial advice before you do that. That is a very, very big decision to make at what is the bottom of a very volatile market.

Q221 **Ms Eagle:** I will just interrupt you there, Chris. The FCA said that it was worried by 80% of the firms that are giving advice in this market. It is clear from figures you have provided that there is a huge bias in the pensions freedom market for companies to advise individuals to go into drawdown, rather than buy annuities or do other things. Are you keeping a special eye on all of that? You were going to publish investment pathways, but obviously that has been put off because of the coronavirus emergency, which means that more people will be at risk of scams and mis-selling.

Christopher Woolard: There are multiple points within your question. First of all, the 80% relates to DB transfers advice in one particular sample that we took, which we published a while ago, and we expressed real concerns about that market. Work around DB transfers and how they are regulated will continue. That is one of the things we said in our business plan is an important part of the work that we have ongoing aside from the current emergency, so we still will be acting in that space. We have a number of questions about investment pathways, and we still think they are the right answer. The question is just, can you implement a change that significant at a time when there is this much disruption? That is the reason for putting it off a few months, but we still think they are the right answer.

In the meantime, there are questions about people being open to scams. We are working very actively not just with the Pensions Regulator but with the NECC, the NCA and the police around how we act on scams in the current environment. We have seen good financial advice given in general around most markets. DB transfers were a real exception, but we have seen good advice given around most advice markets. Where individuals are really thinking about cashing in all their investments right now, in the current crisis, our best advice still would be: go and see a regulated financial adviser, because deciding to sell up at the moment, when the market is at a bottom point, is probably not going to be the right thing for the vast majority of consumers.

Ms Eagle: Thank you.

Q222 **Chair:** Chris, before we pass on to the final set of questions from Harriett, I know that Rushanara had hoped to ask you before you dropped out whether the mortgage holiday arrangements would also apply to mortgage prisoners. Can you confirm that? Sam felt that it did, but we wanted to hear from you.

Christopher Woolard: It is complex. Where a so-called mortgage prisoner is in one of these unregulated books but there is a regulated administrator sitting over the top of that book, which is the majority of individuals we are talking about, we read our rules on mortgage holidays to read through into that. So there is an expectation that the 90-day so-called holiday would be given on application, and the expectations we have around no repossessions during the period of the crisis will also apply. For those who are completely unregulated—in other words, there is no regulated administrator necessarily sitting over the top of them, and certainly the firms themselves are not within the regulatory perimeter—we have said that in the current crisis, we expect, really as a moral question, particularly the piece around no repossessions to apply. Indeed, where there are senior individuals in those unregulated businesses who might at a later point in their career apply for a senior management role within a regulated firm, we are going to take that into account in assessing their fitness and properness.

Chair: Thank you. That is very clear. I will move to Harriett now. We are fairly tight on time, I am afraid.

Q223 **Harriett Baldwin:** I will try to be as quick as possible. Chris, I want to start with you, while we have got you, and ask about insurance. You sent a very helpful letter today to the insurance industry, saying what your expectations were for how they should treat their customers. I wondered whether you had seen any examples of insurance companies that you feel had not been treating their customers fairly.

Christopher Woolard: What we have seen so far, and we have been talking to the insurance industry a lot during the crisis, is three broad things in the insurance industry. First, in most cases, they are working hard to pay out claims, and in some difficult circumstances—so we are seeing firms doing the best they can in difficult circumstances, whether that is to do with travel or business interruption, and in all sorts of places.

In the second group that I would describe, we have seen firms getting valid claims, particularly on business interruption insurance, for example. What we have said to all firms is, "You need to be thinking about how you are paying out against those claims as quickly as possible." A lot of firms have said, "Where we can, we will make interim payments or, if it's quite a small amount, we will just settle right now, and not wait for the end of the crisis", but we have seen some that have decided to keep going, saying, "Let's wait until the end of the crisis before we can work out what we need to settle up the claim." We think that interim claims should be settled as quickly as possible by those firms.

In the third group, we know there will be disputes potentially between small firms and their insurers, particularly on business interruption insurance but also on a number of other things. There, we have reminded firms that the Financial Ombudsman Service is available—that is a quick route for settling those kinds of disputes and, if there is a dispute, we expect it to be settled as quickly as possible.

Q224 **Harriett Baldwin:** It sounds as if the grey areas for small businesses can be referred to the financial ombudsman. Are you finding that some of that grey area is around business interruption and the question of the notifiable disease, and covid-19 being a new disease?

Christopher Woolard: There is a range of issues here. One of the issues we have, particularly with small firms and their insurers, is that it is a brokered market and quite a highly tailored one. It is not as if we have hundreds of standardised policies; what we have are some quite bespoke policies, so the devil is really in the detail. But there are, as you put it, grey areas here where certainly the person who has been insured believes they might be covered, while the insurer perhaps believes they are not, and the ombudsman provides a fast route for dealing with those kinds of issues.

Q225 **Harriett Baldwin:** Are you happy that the ombudsman is staffed up? What are you seeing with the staffing levels of the insurers themselves? Are they able to pay out legitimate claims quickly at the moment?

Christopher Woolard: Insurers are experiencing the same kinds of issues that we were talking about earlier in the session with banks. They have call centres up and running, but they have sickness rates of somewhere about 15% or slightly more. They are clearly working through some difficult issues at the moment with their own people, but they have got sufficient resource in place to pay claims and to pay claims quickly, wherever they possibly can.

On the ombudsman side of this equation, Caroline Wayman and I have spoken briefly throughout this. The ombudsman is fully operational, as is the FCA, and they are ready and able to assist, should people want to go down that route.

Q226 **Harriett Baldwin:** I will switch over to Sam now and to the solvency of the insurance sector. You said at the beginning of the evidence that the sector went into the crisis very solvent. I know that you have encouraged some of them to avoid paying dividends—you have been putting some pressure on the industry in that regard. Do you feel that any companies in the sector will suffer from a solvency problem?

Sam Woods: As you say, going into the crisis, they went in well capitalised. The first hit for them is the financial markets here—we have had these enormous movements in financial markets—and they have broadly weathered that quite well. It leaves them with a coverage ratio relative to their capital requirement broadly in the range of 130% to 160%, so 30% to 60% more capital than we say they need in order to be sure that they can meet a further stress. That is down from a range between not down at all to down up to 20 percentage points of coverage through this stress.

There has also been a bit of liquidity stress during this market turbulence, because people have to meet collateral calls from the banks where they have hedged risk through derivatives, and some of that has put some strain on, but that is all being managed.

The main two issues that we are focused on now are, first, the prudential side of the general insurance stresses. As firms need to make good on business interruption policies they have written—the sort of thing that Chris was writing about to the firms today, travel and so on—that will obviously cost them. We think we have that covered in capital requirements and provisions, but you never know until the thing flows through completely.

The other is more on the life insurance side, the topic we touched on earlier of corporate downgrades, which have been happening already, and defaults. Those are painful because insurance companies hold bonds from those companies and, as those things happen, they become worth less, but their capital requirement and their technical provisions adjust as well. We are having to work through that with those companies. Again, we should have captured that in the stress testing that we do already to set their capital requirement, but we want to work through it and see whether we have really got it all, and that is what we are doing at the moment.

Q227 **Harriett Baldwin:** This is the technical issue around the transitional measures on temporary provisions and the smoothing of the solvency. Without that, would you have some insolvencies, do you think?

Sam Woods: No, we certainly wouldn't have insolvencies. The TMTP that you mentioned has alleviated the strain of the financial market stresses a bit, but I do not want to overdo it. It is a few percentage points relative to those numbers I was giving you. The other piece of machinery that is operating quietly in the background is the thing we have discussed in Committee before, the matching adjustment, which effectively shields life insurance companies in particular from blow-outs in bond spreads that are driven by liquidity. That has softened the blow somewhat; it is probably doing a more important job than the TMTP at this stage.

Q228 **Harriett Baldwin:** But, again, you do not feel that without it there would be actual insolvencies?

Sam Woods: No, I don't think we would have insolvencies, but the matching adjustment is a major part of our regime. To give you a sense, the matching adjustment figures for end 2018—the latest ones we have on a consistent basis across the industry for publication—show £68 billion of benefit. That is pretty significant, and if that somehow went away, it would be a major problem, but we have no intention of taking it away.

Q229 **Harriett Baldwin:** My final questions are really for both of you. I would imagine there will be a demand in future for companies to buy pandemic insurance, to strengthen their ability to bridge an event such as this. No doubt there will be companies willing to offer pandemic insurance. Do you think that is going to become a viable market? Do you think it is something that is going to need a Pandemic Re role from Government? What are your views on how the insurance market will evolve in the future after this shock?

Sam Woods: Perhaps I will make a brief comment, as I have the mic, and then pass to Chris. That is something that is being talked about by several of the players in the London market at the moment. Of course, with a pandemic, the clue is in the name: the reason it is excluded from many policies is that it is not possible to diversify away in a way that you can diversify away some other things. It is not as readily insurable as many other sorts of risk—it is insurable to a degree, but perhaps less so than some other things. It is an interesting question whether, like Flood Re and Pool Re, this is an area where it makes sense to have some kind of Government-backed or Government-associated pooling of risk, but unfortunately, if that idea comes to pass, it is too late for this time around. It might help us next time around.

Christopher Woolard: As Sam says, that is an interesting idea. It has clearly been talked about at length. One of the big questions is whether that is the only way that the market can cope with that level of risk. I think that in the short term we will see, as we did after SARS and those kinds of incidents, firms seeking to write that out of their standard cover very quickly. That will be the most immediate reaction that we see. But there will be a demand for this in the market, as you say, and it may have to go down the same kind of route as terrorism or other events that are very difficult for the market to absorb on its own.

Harriett Baldwin: Thank you.

Chair: I thank everybody for joining in this session, and particularly our three witnesses in the panel that we have just had. We have seen the marvels of technology that mean we can all meet, but we have also seen some of the downsides. I certainly disappeared at one point and Chris disappeared for quite a while—although you did make up for it with the cameo appearance that came through the door behind you during one of your contributions.

Thank you very much. I echo one comment that has been made by at least a couple of Members today by expressing our appreciation for all the extraordinary hard work that you are putting in at the moment. I personally thank you for the way in which your institutions have kept me and the Committee closely informed on all the kinds of issues that we have been discussing—they are immensely important at the moment. I thank you for all that you are doing in this very difficult time. On that note, the session is now concluded.