

## **Alert** | Financial Regulatory & Compliance / Real Estate



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### **Non-Bank Lending in the Spotlight: UK House of Lords Inquiry into Systemic Risks and Market Stability**

In July 2025, the Financial Services Regulation Committee of the House of Lords (the Committee) commenced an inquiry into the growth of non-bank lending. A particular focus of the inquiry is on whether the developments in bank regulation following the global financial crisis (GFC), particularly enhanced capital and liquidity standards, have inhibited the amount of bank lending to the “real economy” in the UK, leaving non-bank financial institutions (NBFIs) to satisfy the unfulfilled demand for credit, and if that is the case, what the financial stability implications of this are.

NBFIs existed before the GFC. Securitisation vehicles, usually established by banks, were the most visible NBFIs at that time, though by no means the only ones. The growth of securitisation as a financing tool in the two decades preceding the GFC enabled the distribution of risk across different global markets, with effects that continue to affect the financial landscape. Towards the end of this period, one or more loans included in securitisations were tranching into a “securitised portion” and a “non-securitised portion,” with the latter ranking subordinate to the former, and being held by investment funds, another category of NBFI, that wanted to invest in a particular loan and had a greater appetite for risk.

When the assets underlying any form of securitised debt product deteriorate, the securitised debt product necessarily deteriorates, albeit to different extents. This meant that banks and other investors found that the AAA or AA-rated securitised debt products they had invested in and that they had regarded as safe

were not, and that secondary market prices and ultimately liquidity for these products declined and then disappeared, causing losses of a severity that could not have been foreseen. The impact on the non-securitised portions of loans was more severe still. The impact on credit availability, and the effect on the real economy, was mitigated through central bank intervention, reducing interest rate and purchasing “troubled assets.”

The current generation of NBFIs are not the same as the pre-GFC ones. In addition to insurance companies and pension funds, some are structured as close-ended investment funds in the form of limited partnerships, managed by professional managers with a specific investment mandate from their investors. Some have no leverage. Others have bank-provided leverage, through so called “loan on loan” financings or repo financings. Others still, particularly in the corporate and leveraged loan markets, finance themselves using securitisation, specifically Collateralised Loan Obligations or CLOs. Some use leverage not just at the level of the assets but at the level of the investment fund, in the form of subscription lines or NAV facilities. Some provide mezzanine debt or preferred equity, which is combined with senior debt that bank lenders provide. Complexity, both in terms of assets and in terms of capital structures, is evolving.

### **Regulatory Transparency and Market Inter-Connectedness: Key Focus Areas**

The investigation of the Committee will focus on, but will not be restricted to:

- whether the enhanced regulation of banks following the GFC, particularly related to capital and liquidity requirements, has had an impact on bank lending to the “real economy” in the UK. This is, from a public policy point of view, a significant consideration because without access to competitive, stable finance, UK economic recovery may be stifled;
- the inter-connectedness between NBFIs, banks, and other regulated financial market participants. This inter-connectedness was evidenced during the GFC when banks holding securitised debt products as part of their trading books or that they had warehoused in the expectation of distribution, had to sell them into a rapidly declining secondary market, suffering severe losses and insurers who had sold credit protection in respect of securitised debt products through credit default swaps or monoline insurance policies, had to make payments to their counterparties as payment defaults occurred;
- whether there is sufficient information about the activities of NBFIs available to the UK regulators or whether there is a need for greater transparency. While the importance of regulatory reporting for the identification and management of risk should be recognised, the impact of extensive reporting requirements on NBFIs and their borrowers should also be borne in mind;
- whether NBFIs pose systemic risks to the UK’s financial system and if so, how these can risks be mitigated. From a public-policy perspective, this is an important question if the lessons of the GFC are to be learned; and
- whether and if so, to what extent NBFIs have an advantage over banks in providing credit to the UK economy given the difference in their regulatory obligations and if so, should consideration be given to regulatory equality between NBFIs and banks.

These are important questions, not just for banks and NBFIs as providers of credit to a variety of sectors of the real economy (principally, small and medium sized enterprises, commercial and residential real estate developers and investors, infrastructure developers, investors, and private equity owned businesses), but also for users of credit, particularly where efficient and stable leverage is a critical element of a business plan. A diverse and liquid commercial credit market is important for the UK, and given that UK-based lenders and borrowers are active across Europe as well, important for Europe.

The inquiry is in the process of gathering evidence. It is undertaking meetings (open to the public and available online) with individuals who have knowledge of the non-bank lending markets and it is also inviting written submissions from a wider group. A number of these meetings have already taken place. As a result of the work of the Committee, the regulatory requirements applicable to NBFIs may evolve in some way.

### **FCA Oversight and Future Regulatory Developments for Non-Bank Lending Markets**

At the same time, the Financial Conduct Authority (FCA) has also been reviewing private market lending activity and seeking detailed information from large market participants. The FCA has been particularly focussed on valuation practices and conflicts management practices and has been issuing detailed feedback about good and poor practices it has encountered among market participants. The FCA is also focussed on the risks linked to the use of leverage, and in particular concentrated leverage, where a leveraged NBFIs is heavily interlinked with a systemically important institution.

GT will monitor these developments.

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