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The UK's House of Lords Reports on Concerns About Private Market Exposures

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By Alix Prentice
Partner | Financial Regulation

On 9 January the Financial Services Regulation Committee of the UK Parliament's House of Lords published its report on "**Private markets: Unknown unknowns**" (the **Report**). Set in the context of a growth in global private markets (which term generally refers to private equity and private credit funds, but includes all forms of non-bank financial intermediation including venture capital, private real estate and infrastructure finance) from less than $4 trillion in AUM in 2008 to around $16 trillion as at the date of the report (with $185 billion of that AUM in the UK) the Report focuses, unsurprisingly, on what concerns around the rapidity of this growth, the significant degree of interconnectedness between private markets and banks and insurers, and weakening lending standards means for UK financial stability. Importantly, though, the Report also flags how unintended consequences of the post-GFC bank capital reforms from 2008 onwards have led to a squeeze on the availability of credit for SMEs which has affected growth, as well as contributed to the exponential rise of provisioning of finance through private market channels.

Given the rapidity of this change, the Report makes a number of broad recommendations, many of which are self-evident. Of note:

1. It examines the increasing use of significant risk transfers by banks, as well as an appetite in the market for securitising private credit, and urges the Bank of England and Prudential Regulation Authority (**PRA**) to "*pay close attention to the development of these markets*";

2. SMEs (businesses with at least two of a turnover of less than £54 million, a balance sheet of less than £27 million, and fewer than 250 employees) are currently showing a limited appetite to borrow. While the private credit market does not appear to be exploring the SME market, the Report urges the PRA to look at how changes to the capital regime could be made to maximise the amount available to support lending to SMEs.

3. The Report generally urges the Government, the Bank of England and the relevant regulators to get a swift grip on the information available on sector-by-sector lending. While it recognises that the Bank of England is conducting its System Wide Exploratory Scenario (which explores how the UK financial system would respond to a market shock) on a voluntary basis, it recommends that the Government keeps the powers available to the Bank under review, contingent on its outcome;

4. Finally, the Report expresses concise concern that the UK Government (HM Treasury) does not have a firm grasp on "*the emerging issues related to private markets and their potential impact on financial stability"* and is overly passive.