Bank of England

Financial Stability Report

Financial Policy Committee
December 2025

Bank of England

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Presented to Parliament pursuant to Section 9W(10) of the Bank of England Act 1998 as amended by the Financial Services Act 2012.

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The primary responsibility of the Financial Policy Committee (FPC), a committee of the Bank of England, is to contribute to the Bank of England's financial stability objective. It does this primarily by identifying, monitoring and taking action to remove or reduce systemic risks, with a view to protecting and enhancing the resilience of the UK financial system. Subject to that, it supports the economic policy of His Majesty's Government, including its objectives for growth and employment.

This Financial Stability Report sets out the FPC's view of the outlook for UK financial stability, including its assessment of the resilience of the UK financial system and the main risks to UK financial stability, and the action it is taking to remove or reduce those risks. It also reports on the activities of the Committee over the reporting period and on the extent to which the Committee's previous policy actions have succeeded in meeting the Committee's objectives. The Report meets the requirement set out in legislation for the Committee to prepare and publish a Financial Stability Report twice per calendar year.

In addition, the Committee has a number of duties, under the Bank of England Act 1998. In exercising certain powers under this Act, the Committee is required to set out an explanation of its reasons for deciding to use its powers in the way they are being exercised and why it considers that to be compatible with its duties.

The Financial Policy Committee:

Andrew Bailey, Governor
Sarah Breeden, Deputy Governor responsible for financial stability
Clare Lombardelli, Deputy Governor responsible for monetary policy
Dave Ramsden, Deputy Governor responsible for markets and banking
Sam Woods, Deputy Governor responsible for prudential regulation
Nathanaël Benjamin, Executive Director of financial stability strategy and risk
Nikhil Rathi, Chief Executive of the Financial Conduct Authority
Stephen Blyth
Jon Hall
Randall Kroszner
Liz Oakes
Carolyn Wilkins
Gwyneth Nurse attends as the Treasury member in a non-voting capacity.

This document, unless otherwise stated, uses data available as at 24 November 2025.

The ‘Results of the 2025 Bank Capital Stress Test’ section and Boxes E and F have been produced by Bank staff under the guidance of the FPC and Prudential Regulation Committee (PRC). They set out the judgements and actions taken by the PRC and FPC that were informed by the test results and analysis.

Annex 2 of this Report, setting out the individual bank results and qualitative narrative, have been formally approved by the PRC.

The sections and annexes were finalised on 25 November 2025, except Section 5, Boxes E and F and Annexes 2 and 3 which were finalised on 1 December 2025.

PowerPoint™ versions of the Report charts and Excel spreadsheets of the data underlying most of them are available at **www.bankofengland.co.uk/financial-stability-report/2025/december-2025**.

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Financial Stability Report Summary

The Financial Policy Committee (FPC) seeks to ensure the UK financial system is prepared for, and resilient to, the wide range of risks it could face so that the system is able to absorb rather than amplify shocks and serve UK households and businesses.

The overall risk environment

Risks to financial stability have increased during 2025. Global risks remain elevated and material uncertainty in the global macroeconomic outlook persists. Key sources of risk include geopolitical tensions, fragmentation of trade and financial markets, and pressures on sovereign debt markets. Elevated geopolitical tensions increase the likelihood of cyberattacks and other operational disruptions.

In the FPC's judgement, many risky asset valuations remain materially stretched, particularly for technology companies focused on Artificial Intelligence (AI). Equity valuations in the US are close to the most stretched they have been since the dot-com bubble, and in the UK since the global financial crisis (GFC). This heightens the risk of a sharp correction.

The role of debt financing in the AI sector is increasing quickly as AI-focused firms seek large-scale infrastructure investment. By some industry estimates, AI infrastructure spending over the next five years could exceed five trillion US dollars. While AI hyperscalers will continue to fund much of this from their operating cash flows, approximately half is expected to be financed externally, mostly through debt. Deeper links between AI firms and credit markets, and increasing interconnections between those firms, mean that, should an asset price correction occur, losses on lending could increase financial stability risks.

Credit spreads remain compressed by historical standards. Two recent high-profile corporate defaults in the US have intensified focus on potential weaknesses in risky credit markets previously flagged by the FPC. These include high leverage, weak underwriting standards, opacity, complex structures, and the degree of reliance on credit rating agencies, and illustrate how corporate defaults could impact bank resilience and credit markets simultaneously.

While the impact of these specific defaults has been limited, a diverse range of financial market participants were exposed. Such diversity can help absorb risks, but opacity around the extent of exposures, and their possible interconnections, can also create uncertainty about how widely shocks in credit markets can propagate. It is important that market participants have a clear understanding of their exposures, including in stress scenarios where correlations and losses can shift outside historical norms. Market participants should also ensure that underwriting standards are robust and that they do not over-rely on credit ratings as a substitute to carrying out appropriate due diligence.

Private markets have grown significantly in the UK over the past two decades and are an important source of funding for corporates. While resilient to date, the private markets ecosystem has not been tested through a broad-based macroeconomic stress at its current size. In order to enhance understanding of the broader risks and dynamics of private markets, the FPC supports the next system-wide exploratory scenario (SWES), focused on the resilience of the private markets ecosystem.

Public debt-to-GDP ratios in many advanced economies have continued to rise this year. Governments globally face spending pressures, given the context of changing demographics and geopolitical risk, potentially constraining their capacity to respond to future shocks. Significant shocks to the global economic or fiscal outlook, should they materialise, could be amplified by vulnerabilities in market-based finance (MBF), such as leveraged positions in sovereign debt markets.

As an open economy with a large financial centre, the UK is exposed to global shocks, which could transmit through multiple, interconnected channels. Stress in one market, such as a sharp asset price correction or correlation shift, could spillover into other markets. Simultaneous de-risking by banks and non-banks can lead to fire sales, widening spreads and tightening financing conditions for UK households and corporates. Market participants should ensure their risk management incorporates such scenarios.

UK household and corporate aggregate indebtedness remains low. The UK banking system is well capitalised, maintains robust liquidity and funding positions, and asset quality remains strong. The results of the 2025 Bank Capital Stress Test demonstrate that the UK banking system is able to continue to support the economy even if economic and financial conditions turn out to be materially worse than expected. This underscores the role of financial stability as a pre-condition for sustainable growth.

As part of ensuring the UK banking sector is both resilient and able to support growth, the FPC has reviewed its assessment of the appropriate level of bank capital requirements (published alongside this FSR, for further details refer to **Financial Stability in Focus: The FPC's assessment of bank capital requirements**). The Committee judges that the benchmark for system-wide Tier 1 capital requirements**, previously judged to be around 14% of risk-weighted assets (RWAs), is now around 13% of RWAs.** That judgement is consistent with the evolution in the financial system since the FPC's first assessment in 2015, including a fall in banks' average risk weights, a reduction in the systemic importance of some banks and improvements in risk measurement.

The FPC and sustainable growth

Maintaining financial stability is essential to supporting sustainable economic growth over the long term. A stable financial system supports lower risk and term premia, lowering the cost of borrowing and improving incentives to fund long-term productive investment. In line with its remit, the FPC

seeks to maintain financial stability by identifying, monitoring, and addressing systemic risks to the financial sector – including those set out in this Report – so that the financial system can support the UK economy in both good times and bad.

In response to the Chancellor's request in the FPC's **November 2024 remit letter**, the FPC has assessed and identified areas where the financial sector could contribute further to supporting sustainable growth through higher productivity growth, investment and innovation. The financial sector plays a role in contributing to productivity growth by providing vital services to UK households and businesses, including the provision of financing for investment in capital and technology. But there are a broader range of factors across the economy at play in driving productivity growth, such as trade conditions, scientific and technological innovation, and human capital.

Lending to UK households and corporates has in the past fluctuated due to changes in financial and macroeconomic conditions. Incentives in the financial system led to unsustainable lending growth in boom times followed by periods of deleveraging during the resulting downturn. However, post-GFC regulation has increased bank resilience. Combined with the FPC's use of the countercyclical capital buffer (CCyB) in stress, this has enabled the banking sector to continue to support households and businesses through recent shocks to the economy.

Lending to small and medium-sized enterprises (SMEs) has been weak since the GFC, reflecting both the small share of SMEs seeking credit and historical barriers these firms face in accessing finance. These barriers are not unique to the UK, with SMEs across many economies facing similar challenges. New lenders that have entered the market over the past decade are increasing their share of SME lending, particularly for SMEs which do not meet the appetite of larger lenders. For further detail refer to Box B of the FSR.

The FPC has already taken steps to ensure that its resilience-building measures are implemented efficiently as the financial system evolves. Recent examples of this include reducing the frequency of its main Bank Capital Stress Tests to every other year and recommending an amendment to the implementation of its loan to income (LTI) flow limit to allow individual lenders to increase their share of lending at high LTIs.

The FPC has undertaken work to assess and identify areas where there is potential to increase the ability of the financial system to contribute to sustainable economic growth, and potential solutions to the impediments the sector might face in doing so (refer to Box A for more details). These include barriers faced by pension funds and insurers in supporting long-term capital investment in the UK economy; challenges high-growth firms face in accessing domestic finance at larger funding rounds; and issues in the financial sector's responsible adoption of innovative technology. The FPC supports:

- The changes made by the Prudential Regulation Authority (PRA) to Solvency II to encourage investment in productive assets by UK insurers, particularly through its reforms to the Matching Adjustment (MA) regime and its introduction of a Matching Adjustment Investment Accelerator

(MAIA). This should support delivery of the UK insurance industry's commitment to invest £100 billion in UK productive assets over 10 years.

- Work to ease impediments to high-growth firms accessing funding, including use of public-private partnership funding initiatives to channel financing to these firms and the broader population of SMEs to support productivity improvements, and supporting the working group on lending backed by intellectual property established as part of HM Government's Industrial Strategy.
- Efforts by authorities and industry to support the UK financial system's adoption of innovative technology, including through the National Payments Vision, the Bank's AI consortium and the Financial Conduct Authority's (FCA's) AI Lab's Live Testing service.

The FPC remains committed to identifying further ways in which it can deliver on its objectives to support sustainable economic growth.

For further details refer to Section 1 and Box A of the FSR.

UK households and corporates

UK household and corporate aggregate indebtedness remains low. The share of households in arrears on their borrowing or with high debt-servicing burdens is low by historical standards. However, some groups are more vulnerable to economic shocks than others, with renters remaining under pressure. In line with easing monetary policy and a competitive mortgage market, quoted mortgage rates have continued to decrease. And, continuing the trend from July, growth in mortgage lending has risen to 3.2% year on year, above the post-GFC historical average of 2.2%.

Mortgage lenders have been adjusting their behaviour following the March 2025 clarification of the FCA's Mortgage Conduct of Business (MCOB) rules and recent changes in the FPC's recommendation on how to implement its LTI flow limit. While it remains too early to assess the full impact of these policy changes in the mortgage market, recent indicators suggest a higher supply of credit to households with net mortgage approvals reaching a nine-month high.

The corporate net debt-to-earnings ratio, at 134%, remains well below Covid (166%) and post-GFC (230%) highs. Nevertheless, potential shocks in global financial markets could increase the likelihood of corporate vulnerabilities crystallising, specifically for highly-leveraged corporates. Credit spreads remain tight by historical standards, which means funding conditions for corporates are currently benign. However, a sharp correction or crystallisation of global risks could constrain refinancing options for UK corporates. In markets serving higher-risk borrowers, such as leveraged loans and private credit, a larger proportion of outstanding debt has shorter maturity and therefore requires refinancing over the next few years, leaving corporates in such funding markets more exposed to a tightening of credit conditions or a deterioration in investor risk sentiment.

For further details refer to Section 3 of the FSR.

UK banking sector resilience

The UK banking system remains well capitalised. Major UK banks continue to report robust earnings, and their average price-to-tangible book (PtTB) ratios have increased further above 1 since the July FSR.

The results of the 2025 Bank Capital Stress Test indicate that the UK banking system would be able to continue to support the economy even if economic conditions turn out materially worse than expected, enabling it to contribute to long-term sustainable economic growth. The Bank Capital Stress Test scenario includes a severe global aggregate supply shock, leading to a deep recession across countries and a rise in inflation across advanced economies, with central banks raising interest rates to bring inflation back to target. In the stress test, the aggregate Common Equity Tier 1 (CET1) capital ratio starts at 14.5% and falls to a low point of 11.0% in the first year. No individual bank was required to strengthen its capital position as a result of the test.

At the low point of the stress test, bank capital remains well above the sum of aggregate regulatory minima and systemic buffers. Most of this headroom arises from banks beginning the test with capital in excess of regulatory requirements. The FPC and PRA do not oblige firms to maintain buffers in excess of regulatory requirements.

The FPC has maintained the UK CCyB rate at its neutral rate of 2%. While the global risk environment remains elevated, UK household and corporate aggregate indebtedness remains low. The easing of credit conditions since the FPC's October meeting has been in line with the macroeconomic outlook, with some additional easing in the mortgage market related to policy developments (clarification of FCA MCOB rules and changes in the FPC's Recommendation on how to implement the LTI flow limit).

As part of ensuring the UK banking sector is both resilient and able to support growth, the FPC has updated its assessment of the appropriate benchmark level of capital requirements for the UK banking system.

For further details refer to Section 4 and 5 of the FSR.

The FPC's assessment of bank capital requirements

The Committee judges that the updated appropriate benchmark for the system-wide level of Tier 1 capital requirements is now around 13% of RWAs (equivalent to a CET1 ratio of around 11%), 1 percentage point lower than its previous benchmark of around 14%. Given the reduction in the FPC's benchmark, banks should have greater certainty and confidence in using their capital resources to lend to UK households and businesses.

That judgement is consistent with the evolution in the financial system since the FPC's first assessment in 2015, including a fall in banks' average risk weights, a reduction in the systemic importance of some banks and improvements in risk measurement such as through the forthcoming implementation of Basel 3.1. The judgement is also consistent with the analysis of the

range of capital requirements likely to maximise macroeconomic net benefits in terms of long-term growth. That analysis also suggested that materially lower capital requirements could lead to significant reductions in long-run expected GDP.

The FPC has also considered how the capital framework can be made more effective, efficient and proportionate. As a result:

- With the PRA and international authorities, the FPC will work to enhance the usability of regulatory buffers and so reduce banks' incentives to have capital in excess of regulatory requirements.
- The FPC will review the implementation of the leverage ratio in the UK, to ensure that it functions as intended. Within this, the Committee intends to prioritise reviewing the UK's approach to regulatory buffers in leverage ratio requirements.
- The FPC supports initiatives by the Bank to respond to feedback on interactions, proportionality and complexity in the capital framework. That includes considering how capital requirements related to domestic exposures interact. It also includes: developing a systematic approach for updating regulatory thresholds; contributing to HM Government's review of ring-fencing; and responding to feedback received on the PRA's discussion paper on internal ratings-based models for mortgage lending.

This assessment is published alongside the FSR (refer to **Financial Stability in Focus: The FPC's assessment of bank capital requirements** for further details).

The resilience of market-based finance

Downside risks to the economic outlook and a potential broader market correction could interact with vulnerabilities in MBF. The interconnected nature of MBF means it can amplify shocks, including through large leveraged hedge fund positions in sovereign debt markets.

Leveraged borrowing by hedge funds in gilt repo markets remains elevated, reaching close to £100 billion in November. Data suggests this activity is related, at least in part, to the popularity of the cash-futures basis trade. A small number of hedge funds account for more than 90% of net gilt repo borrowing, with trades often transacted at zero or near-zero collateral haircuts and at very short maturities and so require regular refinancing. These vulnerabilities, in the context of compressed risk premia in a highly uncertain global environment, increase the risk of sharp moves. Funds could need to deleverage simultaneously in response to a shock if funding conditions tightened to the extent that refinancing became unavailable or prohibitively expensive. This reinforces the need for market participants to ensure the risk management of their positions takes account of potential shocks, including correlation shifts outside historical norms.

In September, the Bank, in close consultation with the FCA, and with input from HM Treasury and the UK Debt Management Office (DMO), published a **discussion paper** evaluating the effectiveness and impact of a range of potential reforms to enhance the resilience of the gilt repo market; such as, greater central clearing of gilt repo and minimum margin requirements on non-

centrally cleared gilt repo transactions. Any structural reforms identified through this work will take time to implement, which underscores the importance of market participants ensuring their own preparedness for shocks.

Private markets have grown significantly in the UK over the past two decades and are an important source of funding for corporates. UK insurers' exposures to private markets have been growing, including through increasing use of funded reinsurance contracts. While resilient to date, private markets have not been tested through a broad-based macroeconomic stress at their current size. The Bank will undertake a SWES focused on risks from the private markets ecosystem.

Two recent high-profile US corporate defaults demonstrated the risks associated with reliance on Credit Rating Agencies (CRAs) – the ratings associated with both corporates remained relatively stable until close to their defaults. Relatedly, there is some evidence (**IMF October GFSR**) of the expansion in recent years of smaller CRAs producing private ratings, including in the US insurance market. Competitive pressures could provide incentives for some CRAs to provide ratings that are designed to win custom. This underscores the risks of firms over-relying on credit ratings providers as a substitute to carrying out appropriate due diligence.

For further details refer to Section 6 of the FSR.

Structural changes in the UK financial system

Heightened geopolitical tensions and continued advances in technology have underlined the critical importance of operational resilience to the provision of vital services to households and businesses. The FPC supports further actions to be taken by firms and financial market infrastructures (FMIs) to build resilience to operational disruption, and by microprudential regulators to continue to strengthen the regulatory framework. In taking steps to build resilience, firms and FMIs should recognise the role they play in supporting confidence in the financial system, and how disruption to vital services could negatively affect saving, investment and economic growth.

The FPC met jointly with the Prudential Regulation Committee, the Financial Market Infrastructure Committee and the FCA to discuss the UK's approach to enhancing the operational resilience of the UK financial system given the heightened threat landscape and increasing pace of technological change. They agreed about the importance of continued co-ordination on these issues. Boards of firms and FMIs should also work with authorities to use the findings of sector-wide exercises and stress tests such as SIMEX and the Cyber and Operational Resilience Stress Test to improve their understanding of actions they can take to mitigate impacts on financial stability. Given the interconnected nature of the global financial system, the FPC supports further international engagement on operational resilience.

The development of new financial products, such as stablecoins, and other distributed ledger technology (DLT) present both opportunities and risks to the UK financial system. The FPC recognises the transformative potential of technology associated with stablecoins and the importance of ensuring that the public can have the same trust in new forms of money as they do in

existing ones. Use of regulated stablecoins could lead to faster, cheaper retail and wholesale payments, with greater functionality, both at home and across borders. The FPC also notes the potential for growth in the provision of funding directly from financial markets and non-bank financial institutions to support the supply of credit to UK households and businesses, even if deposits move from the banking system to stablecoins. In the UK, the Bank and FCA are developing regimes for systemic and non-systemic stablecoins to ensure appropriate resilience. Other jurisdictions, including the US, are also in the process of designing and finalising their regimes. The FPC welcomes work by the Bank to propose a regulatory regime for sterling-denominated systemic stablecoins, and the **consultation paper** published recently on this topic.

The FPC is continuing to monitor developments in the unbacked crypto-asset sector and its interconnectedness with the financial sector and the real economy.

Climate-related risks to financial stability are becoming more proximate, resulting in risks to asset prices and credit quality in severe but plausible scenarios. If investors reprice financial assets rapidly to reflect climate-related risks, Bank staff estimate that the resulting moves in asset prices could be comparable to those moves seen in recent market stress episodes.

As physical risks from climate change continue to increase over the longer term, lower insurance coverage could transfer risks to households, businesses, banks and governments. Supporting insurability through investments in resilience to physical risks from climate change would be beneficial to UK financial stability.

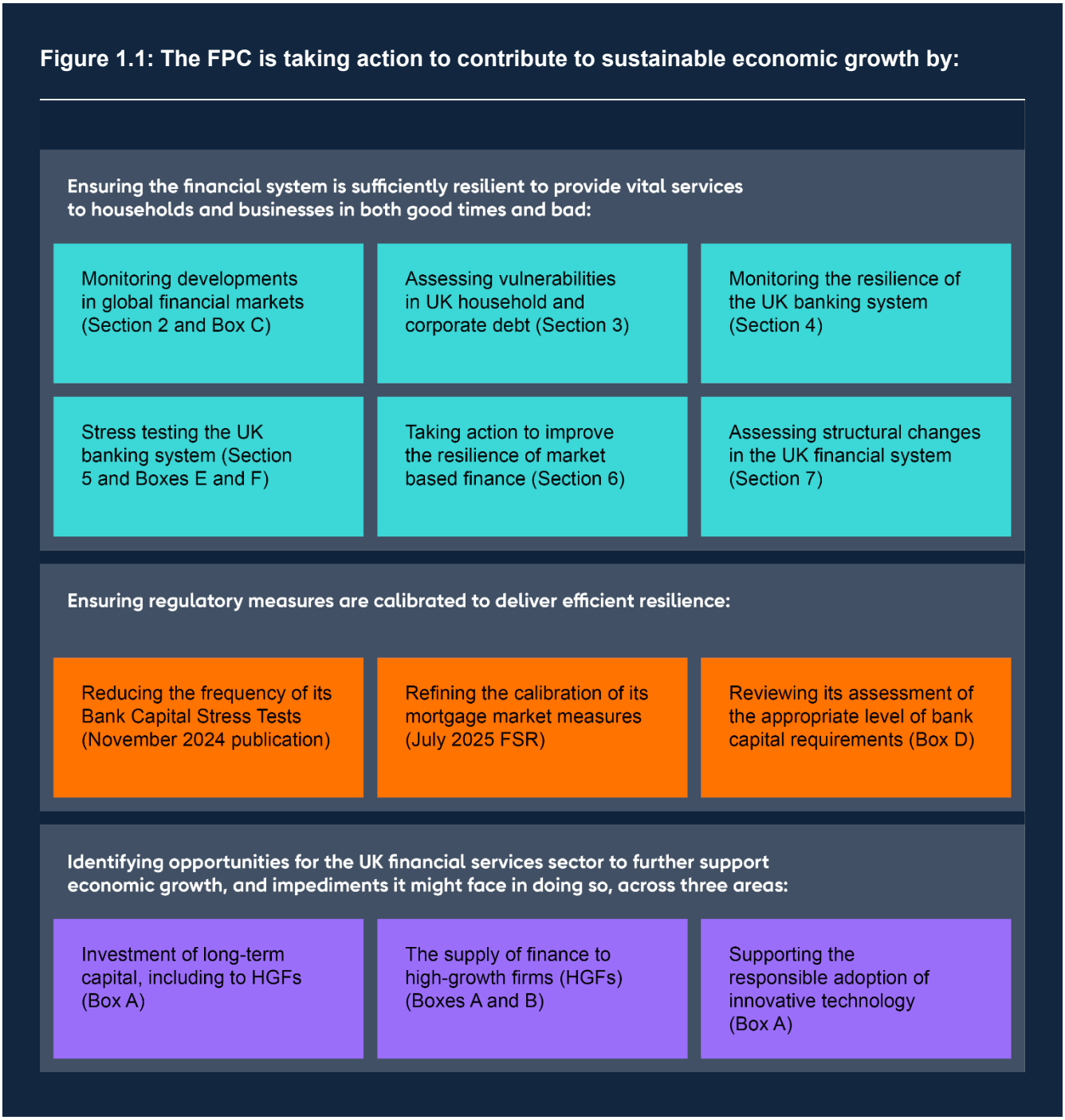
For further details refer to Section 7 of the FSR.

1: In focus – The FPC and sustainable growth

Maintaining financial stability is essential to supporting sustainable economic growth over the long term. In line with its remit, the FPC seeks to maintain financial stability by identifying, monitoring, and addressing systemic risks to the financial sector – including those set out in this Report – so that the financial system can support the UK economy in both good times and bad. In working to advance its primary objective, the FPC continues to take steps to ensure that its resilience-building measures are implemented efficiently and in a way that supports sustainable growth as the financial system evolves.

In response to the Chancellor's request in the FPC's **November 2024 remit letter**, the FPC has assessed and identified areas where the financial sector could contribute further to supporting sustainable growth through higher productivity growth, investment and innovation (Box A). This In focus section sets out how the FPC thinks about sustainable economic growth (Figure 1.1), building on the contents of the **July 2025 Financial Stability Report**.

Figure 1.1: The FPC is taking action to contribute to sustainable economic growth by:



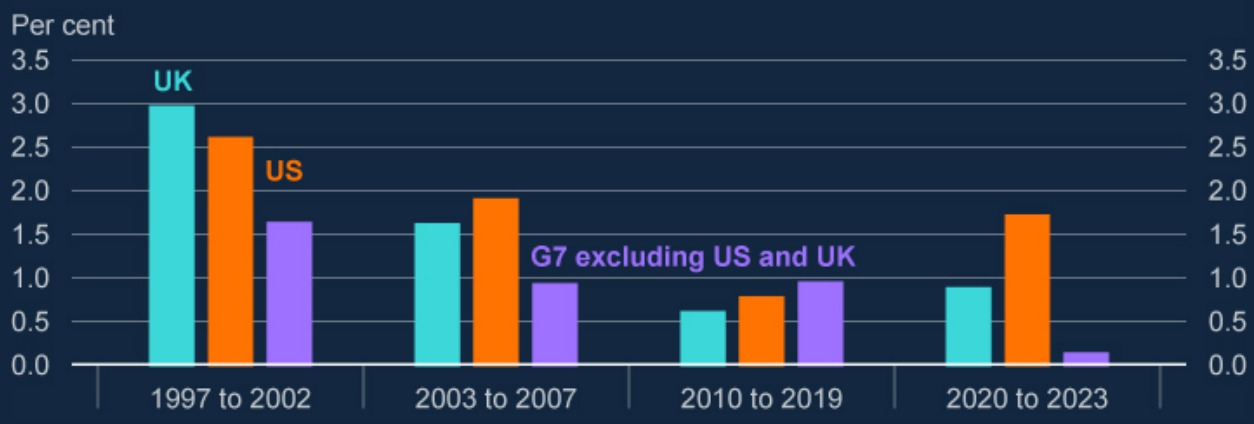
1.1: The role of the financial sector in contributing to sustainable growth

Productivity growth is a key driver of economic growth. Over the past 15 years, UK labour productivity growth has been low by historical standards and relative to some other advanced economies.

In the long term, GDP growth is driven by changes to an economy's supply capacity, which is determined by the amount of labour and capital available, and the efficiency with which these factors can be combined – known as total factor productivity. Labour productivity – measured as output per hour worked – is the main driver of living standards in the long run. Since 2010, UK labour productivity has been low by historical standards and relative to the US. From 2010–19, it was also low relative to other advanced economies (Chart 1.1).

Chart 1.1: UK productivity growth in recent years has been low by historical standards, and relative to some other advanced economies

Average growth in GDP per hour worked, UK, US and G7 excluding US and UK (weighted average) (a) (b)



Sources: OECD and Bank calculations.

(a) Average year on year growth in GDP per hour worked in 2020 US dollars, chain linked volume (rebased), purchasing power parity (PPP) converted. G7 excluding US and UK is weighted by total GDP in 2020 US dollars, chain linked volume (rebased), PPP converted. Weighted average excludes Canada for 1997 due to unavailable 1996 data.
(b) This chart is not directly comparable to Chart 4.1 of the July 2025 FSR due to an update to the underlying OECD database.

In the 1990s, total factor productivity growth in most western economies was high, driven by the diffusion of information and communications technologies such as the internet, which have the characteristics of a General-Purpose Technology (GPT). Past GPTs have been shown to boost productivity for long periods of time, as discussed in a recent speech by **Andrew Bailey**.[1] Evidence shows that productivity growth slowed in the US in the mid-2000s, as it did in other countries including the UK.[2] And **Adler et al (2017)** find that population ageing, slowing human capital accumulation, and lower global trade all contributed to this slowdown.

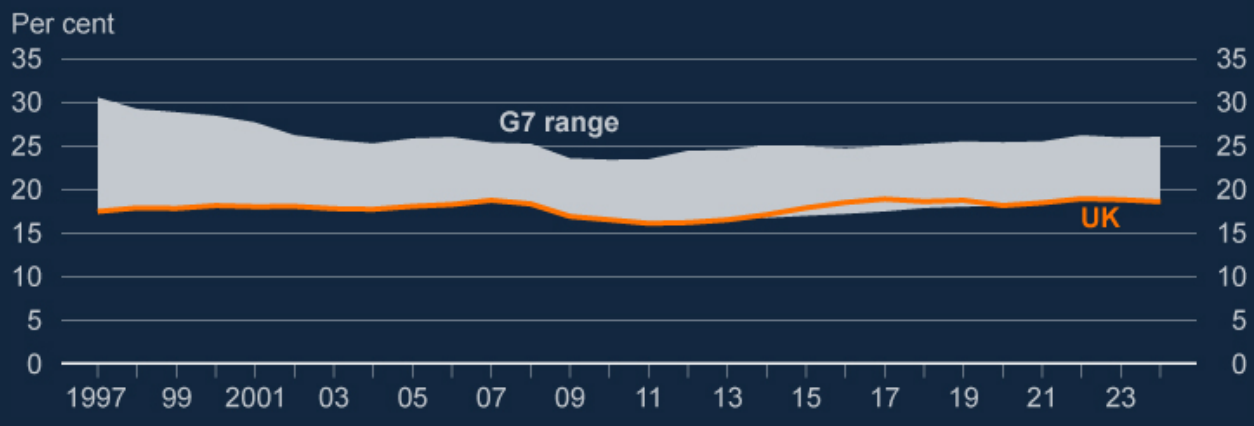
As set out in the **July 2025 Financial Stability Report**, the global financial crisis (GFC) of 2008–09 negatively impacted the provision of vital services including bank lending (Box B), weighing on output and productivity growth. Additional shocks, including the UK's decision to leave the European Union, the Covid pandemic, and the significant rise in energy prices in 2022 following Russia's invasion of Ukraine, have compounded these effects although recent data suggest that the productivity effects of the pandemic have dissipated and there is no longer a significant drag due to the energy price shock. Other G7 countries have seen a similar slowdown in recent years, except the US where productivity growth has picked up since 2020 (Chart 1.1). US productivity growth has increased since the pandemic. There might be a range of reasons for that, but Bank analysis suggests it may partly reflect reallocation of activity and labour towards more productive sectors, and the strength of the US technology sector.

The financial sector plays a role in contributing to productivity growth by providing vital services to UK households and businesses, including the provision of financing for investment in capital and technology. But there are a broader range of factors across the economy at play in driving productivity growth, such as trade conditions, scientific and technological innovation, and human capital. Productivity growth can be accounted for by the level of capital deepening (capital stock per hour worked), and total factor productivity, ie the efficiency with which labour and capital can be combined. These challenges are best addressed by government and businesses, as set out in HM Government's **economic growth**, **industrial** and **infrastructure strategies**, which emphasise the importance to economic growth of public-private partnerships, government investment and other policies such as planning reform.

While the UK has a large and sophisticated financial sector, the UK's level of investment in capital formation as a proportion of GDP is low relative to other G7 nations and has remained among the lowest for many years (Chart 1.2). This could be driven by both demand for finance from businesses looking to invest in capital, as well as the supply of finance to those businesses.

Chart 1.2: Investment in the capital stock is low in the UK relative to other advanced economies and has been for many years

Gross fixed capital formation as a percentage of GDP, UK and G7 range, 1997–2024 (a)



Sources: OECD and Bank calculations.

(a) Gross fixed capital formation includes investment by businesses as well as public sector and dwellings investment.

Factors other than financial regulation have been the primary driver of low investment, and so low productivity. The volume of lending to the UK real economy has been stable as a share of GDP over the long run (Box B). And the FPC has aimed to set a level of bank capital that is likely to maximise macroeconomic net benefits in terms of long-term growth, both in its initial assessment in

2015 and its review this year (Box D). The growth of market-based finance and increased competition within the banking sector have diversified the supply of productive finance to the real economy.

1.2: Growth and the FPC's primary objective

> **Maintaining financial stability is the foundation for sustainable growth. Periods of financial instability – such as the GFC – negatively impact the provision of vital services to households and businesses, weighing on output and productivity growth.**

Because the financial sector plays a role in driving UK productivity growth, actions to support financial stability in turn support economic growth. As set out in the **July 2025 Financial Stability Report**, a stable financial system ensures the provision of vital services to households and businesses, which, in turn, support economic activity including funding, saving, insurance and payment services. These services all support productivity and economic growth.

Financial stability contributes to a stable and predictable economic environment, including by: supporting consumer and business confidence; making the UK an attractive place to do business for international investors; and supporting UK firms' ability to compete abroad. Higher investment by businesses and saving by households increase the available capital for productivity-improving projects. And a stable financial system supports lower risk and term premia, lowering the cost of borrowing and improving incentives to fund long-term productive investment. These factors all facilitate the investment that drives long-term productivity growth (Figure 1.2).

Figure 1.2: A diagram illustrating the benefits of financial stability for productive investment and stable economic growth

The FPC's work on financial stability also supports growth by avoiding the negative consequences of financial instability. Improvements to financial system resilience since the GFC have allowed it to continue to support UK households and businesses through periods of financial stress. For example, UK banks continued to lend to creditworthy households and businesses during recent shocks such as the Covid pandemic, the significant rise in energy prices in 2022 following Russia's invasion of Ukraine, and episodes of market volatility.

> **The FPC primarily contributes to sustainable economic growth by maintaining financial stability. It does so by identifying, monitoring, and addressing systemic risks to the financial sector – including those set out in this report (Figure 1.1).**

A resilient financial system is particularly important given the elevated global macroeconomic risk environment (Section 2), which could pose risks to debt sustainability and GDP growth globally. By monitoring risks to the global economic outlook, the FPC can act to support the resilience of the UK financial system to severe but plausible shocks.

The FPC also monitors household and corporate debt vulnerabilities (Section 3) and the resilience of the UK banking system, which provides the majority of lending to the UK real economy (Section 4). It also stress tests the major UK banks to ensure they are sufficiently resilient to continue to support households, businesses, and growth, even if economic and financial conditions are materially worse than expected (Section 5). Jointly, the resilience of households, corporates and the banking system supports the saving, investment and lending required for sustainable economic growth.

Financial markets are also an important source of funding for UK businesses (Box B). They provide vital financial services which are essential to the daily economic activity of UK households and businesses. Recent periods of financial instability such as in March 2020 and October 2022 demonstrated that vulnerabilities in the system of market-based finance can amplify shocks and affect the provision of vital services to businesses and households. Therefore, the FPC works to improve risk identification in, and the functioning and resilience of, market-based finance (Section 6). The FPC also uses system-wide exploratory scenarios to further understand interconnections between banks and other financial market participants.

The financial system is constantly evolving, and new risks emerging, as technological, economic, geopolitical, and broader societal shifts change the landscape in which it operates. Therefore, the FPC works to identify, assess and respond to structural changes and new risks in the financial system, including through improving macroprudential oversight of operational resilience (Section 7). The FPC takes action to support the responsible adoption of innovative technology by the financial sector. In doing so, the FPC – alongside the Bank – seeks to balance efficiency and resilience, in support of long-term growth.

All of these actions therefore contribute to maintaining a stable and predictable economic environment and creating the necessary conditions for the financial sector to facilitate sustainable growth.

1.3: Growth and the FPC's secondary objective

> **Subject to its primary objective, the Committee has a secondary objective of supporting the Government's economic policy, including its objectives for growth and employment.**

The FPC judges that these objectives are complementary over the long-term: financial stability is necessary for sustainable growth, and sustainable growth supports financial stability – as explained in more detail in the **July 2025 Financial Stability Report**. For example, improvements in productivity growth would ease fiscal pressures and in turn support the resilience of sovereign bond markets globally. As set out in a recent speech by **Jon Hall**, the FPC's mandate balances efficiency and resilience, in support of long-term growth. Further, the FPC's statutory objectives are clear that it should not take any action that would have a significant adverse effect on the capacity of the financial sector to contribute to the growth of the UK economy in the medium or long term.

The FPC has already taken steps to ensure that its resilience-building measures are implemented efficiently as the financial system evolves. The FPC regularly reviews its policy measures; recent examples include **reducing the frequency of its main Bank Capital Stress Tests to every other year** and **recommending** the PRA and the FCA amend implementation of the FPC's loan to income (LTI) flow limit to allow individual lenders to increase their share of lending at high LTIs while aiming to ensure the aggregate flow remains consistent with the limit of 15%.

And the FPC has reviewed its assessment of the appropriate level of bank capital requirements, considering the costs and benefits to long-term growth (Box D). This weighs the macroeconomic costs of capital (which stem from the impact of higher capital pushing up on borrowing costs) against the benefits of capital, which come about because higher bank capital reduces the likelihood and costs of financial crises. In its latest review, the Committee has taken into account the experience of the ten years since it first assessed the appropriate overall level of capital requirements.

Box A sets out the conclusions of the FPC's 2025 work on growth and the financial system. The FPC remains committed to identifying further ways in which it can deliver on its objectives to support sustainable economic growth.

Box A: Conclusions of the FPC's 2025 work on growth and the financial system

In November 2024, via the Committee's **annual remit letter**, the Chancellor asked the FPC to assess and identify areas where there is potential to increase the ability of the financial system to contribute to sustainable economic growth without undermining financial stability. This box updates on the Committee's work, building on the approach set out in the **July 2025 Financial Stability Report**.

> **In response to the Chancellor's commission to identify areas where there is potential for the financial sector to contribute more to sustainable growth, the FPC has identified three areas.**

The FPC agreed in **April 2025** that its work on growth this year would focus on improving the long-term productive growth capacity of the economy by identifying barriers to the provision of credit and vital services to the real economy by the financial services sector. The FPC identified three areas of focus for the work where there is potential to increase the ability of the financial system to contribute to sustainable economic growth without undermining financial stability:

- Investment of long-term capital into assets which increase the productive capacity of the economy, including to high-growth firms (HGFs).[3]
- The supply of debt or equity finance to HGFs including start-ups and scale-ups.
- Supporting the responsible adoption of innovative technology by the financial sector, which has the potential to reshape the UK economy.

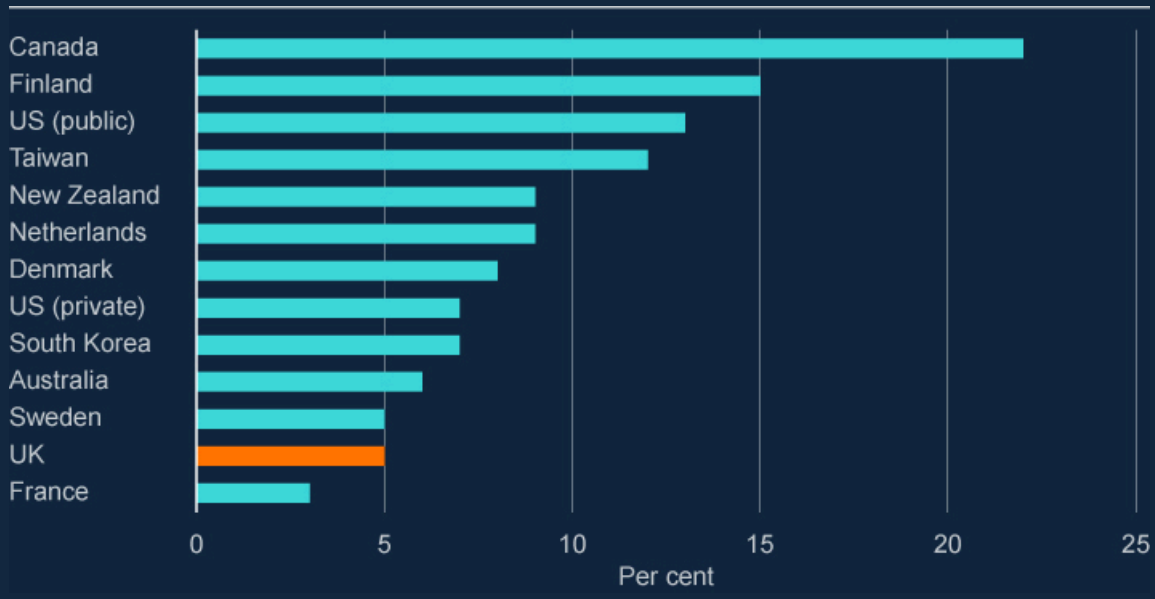
These areas of focus were selected by the FPC as they are directly related to the FPC's remit and are where the FPC judged there to be impediments to the provision of vital services and credit to the real economy. The identified impediments and potential solutions are set out in this box.

To meet the challenges of the future, the UK economy will require a flow of long-term capital to fund investments which improve the infrastructure that supports the economy, fund the development and deployment of new technologies that will drive productivity growth and support the transition to Net Zero. While the UK benefits from substantial international investment as an open economy with a global financial centre, more could be done to identify barriers to domestic investment by UK institutions. UK workplace pension funds have over £2 trillion of assets and the UK life insurance sector has over £2 trillion of assets. But UK defined contribution (DC) pension schemes invest less in assets such as infrastructure, property, and private equity than some of their international peers. For example, UK pension funds allocate around 5% of assets to private equity firms, which are key providers of 'patient capital' including to larger HGFs. This is substantially lower than

some other advanced economies (Chart A). **Research by DWP** estimates that around 22% of UK workplace DC pension assets are invested domestically compared to 44% and 55% in New Zealand's Kiwisaver and Australia's Superannuation systems, respectively.

Chart A: UK pension funds allocate fewer assets to private equity than international peers

Share of pension fund assets allocated to private equity across countries (a) (b)



Sources: New Financial (2024) and The Purposeful Company.

(a) US (private) refers to US private defined-benefit pension funds, and US (public) refers to US public defined-benefit pension funds.
(b) Numbers are not strictly comparable between countries as different subsets of pension funds are captured. Numbers for the UK, Denmark and Finland are system-wide. Numbers for Sweden, South Korea, New Zealand, and Taiwan reflect public reserve pension funds. Numbers for the Netherlands reflect public defined-benefit pension funds, France private defined-benefit pension funds, and Canada all public sector pension funds. Australia captures superannuation funds only.

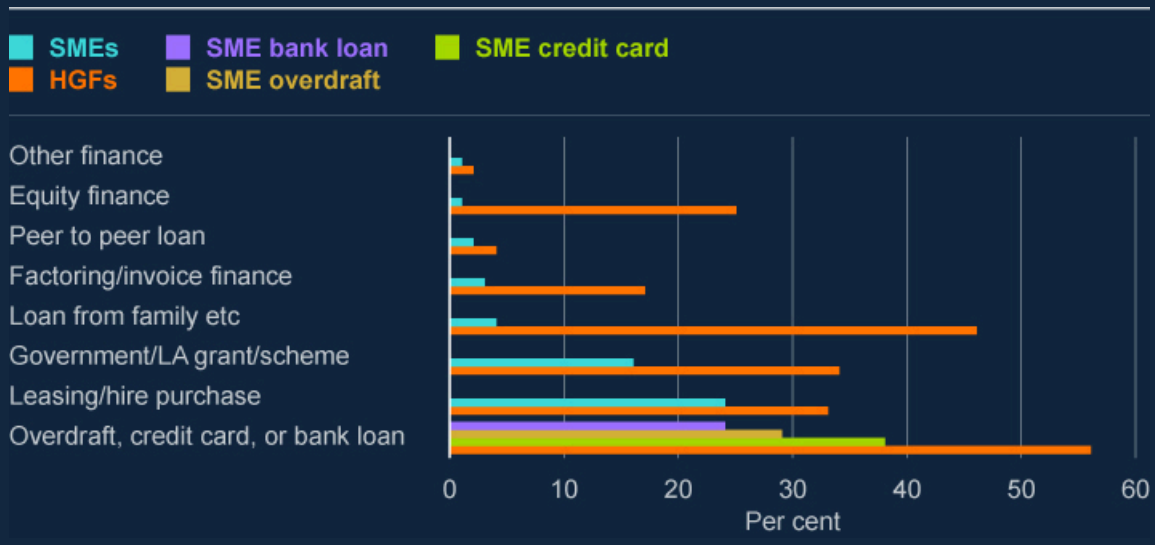
Investment by insurers and pension funds can provide stable sources of capital over the longer term, particularly as their long-term liability structures and investment mandates allow them to hold investments through short-term fluctuations in economic cycles. This provision of 'patient capital' has the potential to benefit long-run economic growth, as well as benefiting insurers' and pension funds' shareholders and policyholders.

The FPC has focused on identifying barriers to the ability of HGFs to access finance because HGFs make an outsized contribution to economic and employment growth in the UK and globally, as set out in a recent Bank staff **literature review**. The **ScaleUp Institute estimates** that while scale-ups account for only 0.6% of the SME population, they contribute more than half of UK SME turnover. And HGFs – including both start-ups and

scale-ups – often represent the frontier in developing innovative ways to deploy both capital and technological innovation. Traditional bank lending is less well-suited to HGFs because, although HGFs are either growing rapidly or have the potential to grow rapidly, they typically have a limited trading history, are not yet consistently profitable, or have low levels of collateral. Consistent with this, staff analysis shows that sectors with more HGFs receive a relatively lower share of new bank lending. Therefore, HGFs are more likely than other SMEs to rely on equity and other finance, such as venture capital (VC) or venture debt, as well as government funding schemes (Chart B).

Chart B: High-growth firms make greater use of equity and other finance, as well as government funding schemes, relative to the wider SME population

Share of HGFs and SMEs using different forms of finance (a) (b)



Sources: Longitudinal Small Business Survey: SME Employers (businesses with 1 to 249 employees) – UK, 2024, and Scale-Up Institute Annual ScaleUp Survey 2024.

(a) Due to the differing nature of both data sets, data is compared where appropriate. For example, the data set covering SMEs splits out the share using bank loans, overdrafts, and credit cards whereas the data for HGFs merges these.
(b) Other finance includes instruments such as **venture debt**.

HGFs often have little collateral aside from intellectual property (IP), which can be hard to use as collateral when borrowing. The **ScaleUp Institute** ranks financing as the third biggest constraint to the growth of HGFs after talent and market access. Actions to ease these constraints, such as supporting the financial sector to provide the breadth and depth of services that HGFs require, can support their growth.

Technological innovation has the potential to reshape the UK economy, boosting productivity, real wages, and economic growth. As set out in the Bank's recent **approach to innovation**, examples include artificial intelligence (AI), distributed ledger technologies

(DLT) and quantum computing. The FPC judges that responsible adoption of technological innovations in the financial sector can deliver benefits to both its primary and secondary objectives. For example, use of DLT could allow for faster and cheaper cross-border payments, reducing inefficiencies within the financial system. The innovative application of new technologies is also central to the UK maintaining its leadership as a global financial centre. However, to ensure the benefits are harnessed in a sustainable way, the risks from such technological adoption must be balanced with the potential opportunities.

The FPC welcomes work by the Bank and other authorities and industry partners to promote innovation in financial services. The Bank and FCA launched the **AI Consortium** on 2 May 2025 to provide a platform for public-private engagement to gather input from stakeholders on the capabilities, development, deployment, and use of AI. The Bank and FCA have also set up the **Digital Securities Sandbox (DSS)**, which provides a regulated environment to encourage innovation in financial market infrastructure.

> **The FPC has identified opportunities for the UK financial services sector to further support sustainable economic growth, and impediments the sector might face in doing so.**

Bank staff, working with HM Treasury (HMT), have conducted a **literature review** and met with more than 50 financial sector, government and academic groups to further understand the impediments HGFs may face in contributing to sustainable growth across the three areas outlined above.

> **UK pension funds and insurers face barriers in supporting long-term capital investment in the UK economy.**

The FPC has identified the following impediments to the investment of long-term capital by pension funds and insurers:

1. **UK DC pension schemes are smaller in scale and allocate less to riskier assets than international peers**. This in a large part reflects the smaller scale of UK DC schemes and a need to shift the focus to long-term value, improved member outcomes and lowering costs as the industry grows and consolidates. Smaller pensions schemes often have less capacity to invest in unlisted productive assets. This can hold back pension schemes from making long-term investments that could fund productive investment in the UK economy. More than four fifths of UK DC pension fund investments are in listed equities, and corporate and government bonds, which represent less than one third of UK and other advanced economy assets. Two thirds of DC schemes do not invest in longer term, less liquid assets at all, and the rest invest only 1.5%–7.0% of their assets, much of which is in real estate.
2. **UK insurers report a lack of opportunities to invest domestically that align to their expertise and risk and reward targets.** This diverts insurers' assets away from productive investments in the UK economy, harming UK growth over the long term.

Potential solutions include scaling up DC pension funds, enabling them to enhance their sophistication and reduce unit costs, thereby improving outcomes for members. DC pension products could also be expanded to offer a wider range of products without daily liquidity which can support longer-term investments. In addition, raising awareness among pension funds and insurers of the opportunities presented by venture and growth finance, including the potential for public-private partnerships, could help address these challenges. Finally, further work to understand behavioural and regulatory barriers to deploying domestic capital into high-growth firms and identify solutions to reduce these frictions is needed.

The FPC welcomes the measures in HM Government's (HMG's) Pension Schemes Bill which aims to address some of these barriers by consolidating the DC pension sector into larger and more sophisticated schemes. Achieving increases in fund size and sophistication should enable these larger DC schemes to access a wider range of asset classes, helping them to deliver better outcomes for their members and the UK economy as a whole.

The FPC supports the changes made by the PRA to Solvency II to encourage investment in productive assets by UK insurers, particularly through its reforms to the Matching Adjustment (MA) regime and its work to deliver a Matching Adjustment Investment Accelerator (MAIA). The PRA published a **policy statement 17/25** on the MAIA on 23 October, which set out the final rules that came into effect on 27 October 2025. The FPC also welcomes the PRA's **discussion paper 2/25 on Alternative Life Capital**, which aims to support innovation in the life insurance sector.

Members of the Association of British Insurers committed to using the Solvency UK reforms to invest at least £100 billion in UK productive assets over the **next decade**. The Bank will continue to work constructively with industry and HMT to explore collectively how UK productive investments can be structured to meet the 'MA' eligibility criteria and thereby be used to their fullest extent. The FPC judges that, if the industry makes use of these regulatory changes to maximise UK productive investments, this will be an important contribution to improving the UK's productivity growth.

The FPC notes the progress made by signatories of the Mansion House Compact, with the proportion of investments in unlisted equities growing from 0.36% in 2024 to 0.6% in 2025. The Committee also notes the Mansion House Accord, in which 17 of the largest UK workplace pension providers have pledged to invest at least 10% of their DC default funds in private markets by 2030, with 5% of the total allocated to the UK.

Building on the progress of the Mansion House Compact, there would be value in further work to identify barriers to allocating funds to HGFs and develop solutions that enable DC pension schemes and other investors to provide productive finance to HGF funding vehicles. The FPC notes the new British Business Bank (BBB) objective, announced in the Autumn Budget 2025, to mobilise institutional capital at scale and the projected participation

of domestic pension funds in the initial £200 million funding round for the BBB's British Growth Partnership Fund. This is an area where the public sector and the private sector will need to work together to find solutions.

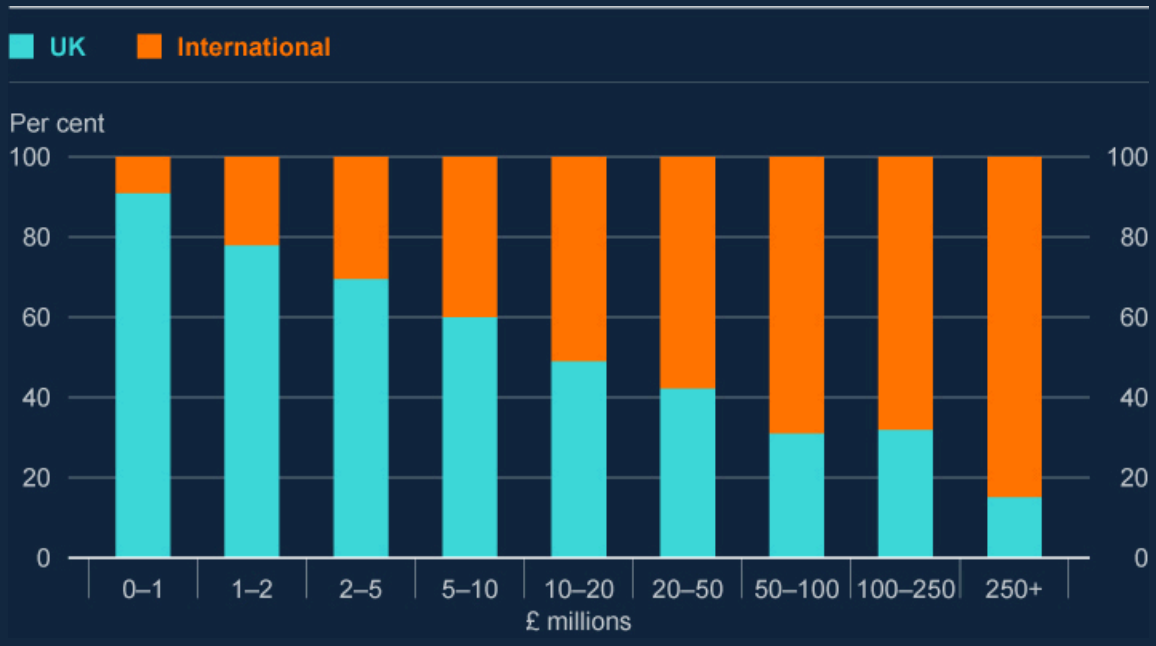
> **HGFs face challenges in accessing domestic finance as funding rounds scale up, navigating a complex funding ecosystem and finding collateral on which to secure lending.**

The FPC has identified the following impediments to the supply of debt or equity finance to HGFs:

1. **HGFs find it progressively more difficult to raise funds** – especially from domestic sources – as funding rounds get larger due to a shortage of **patient capital** (Chart C). While the UK has the third largest VC market in the world and a growing venture debt market, the level of venture investment per capita in the UK is lower than some other advanced economies, including the US. **BBB research** finds that the UK has an investment gap relative to the US, with UK VC investment representing 0.7% of GDP, 10% less than in the US over 2022–24.
2. **HGF finance can be a complex funding ecosystem for funders and founders to navigate.** The fragmentation of financial support services in the UK means there are multiple agencies and schemes, which creates a complex, inefficient landscape that SMEs and HGFs struggle to navigate.
3. **Many HGFs have little tangible collateral, and HGFs struggle to secure lending using IP as collateral.** Banks face significant challenges in developing lending collateralised by IP, primarily due to the difficulty of valuing intangible assets, the lack of standardised frameworks for assessing IP risk, and limited secondary markets for recovery in case of default. Other jurisdictions have developed IP-backed lending markets, but more work is needed to provide a framework for the UK market to develop.

Chart C: The number of domestic investors in high-growth firms' funding rounds declines as the funding round size increases

Percentage of investors in equity funding rounds by deal value (a) (b)



Source: The Purposeful Company, Beauhurst (2024).

(a) For the period 2014–23.
(b) The chart presents the simple count of investors participating in deals of various sizes without weighting or factoring in the amount each investor is contributing.

Easing the impediments to funding HGFs requires a multifaceted approach as no single solution will resolve all the issues HGFs face in accessing debt and equity. The solutions to mobilising domestic long-term capital set out above could benefit HGFs, as could solutions to reduce funding complexity – such as a 'one-stop-shop' for funding information for HGFs. Banks' innovation lending units could also help to address these impediments, for example by working to examine the viability and practicality of IP-backed lending.

The FPC welcomes work done by HMG and other authorities over the past year to ease some of the impediments faced by HGFs in accessing finance, for example, the working group established as part of HMG's **Industrial Strategy** with the aim of removing barriers to IP-backed lending to creative industries. Further, the **Pension Schemes Bill** should help to tackle barriers to investing in VC and venture debt funds that finance HGFs, while HMG's **Business Growth Service** should go some way in making it easier for businesses to navigate the many ways of accessing finance and support.

Reforms introduced this year allow ring-fenced banks to take equity warrants when lending to HGFs, which should make lending to innovative businesses more commercially viable. The Bank is also working with HMT to explore how the ring-fencing regime could be further reformed to allow ring-fenced banks to provide more products and services to UK businesses.

The FPC notes the package of measures to support entrepreneurship announced by HMT in the Autumn Budget 2025. The Committee highlights the importance of enhanced focus on public-private partnership funding initiatives to channel financing to HGFs and the broader population of SMEs, which should support productivity enhancing investment. The FPC notes the important role the BBB could play in this context. Many countries have government sponsored organisations that aim to improve access to finance for smaller businesses and crowd-in private sector investment, like the BBB. These range from Germany's KfW, which provides long-term financing and coinvestment to support SMEs and innovation, to US programs like those run by the Small Business Administration and the State Small Business Credit Initiative, which offer loan guarantees and channel private capital into venture and growth funds. In this context the FPC notes the expanded financial capacity of the BBB this year and the announcement that the BBB will launch 'Venture Link'. Under this initiative the BBB will publish enhanced information on the venture funds it supports and those under consideration, increasing transparency and helping pension schemes identify opportunities.

The Committee encourages more research and policy work on barriers facing HGFs in accessing finance and welcomes the focus of the **Bank of England Agenda for Research, 2025-2028** on growth. This includes analysis of the impediments, and data gaps, to risk-based IP-collateralised lending which is becoming increasingly important to the knowledge economy. The FPC is supportive of the **wor**king group that is exploring how to best support lending to IP-rich sectors.

> **High cyber-resilience costs for tech-reliant firms and the need for modernised UK payment infrastructure are barriers to the responsible adoption of innovative technology in the financial sector.**

The FPC has identified the following issues in the financial sector's responsible adoption of innovative technology.

1. **The technology cost of building and maintaining resilience against cyberthreats is challenging for new and small FinTechs**. The costs of cyberattacks can be large. Elevated geopolitical tensions and continued advances in technology have increased the potential for operational incidents to disrupt the provision of vital services (Section 7). Many cyberattacks have targeted third party suppliers of larger corporates as a way of penetrating their clients' systems. As such a potential point of entry for such attacks, it is therefore important that those suppliers themselves – a number of which can be FinTechs – have robust cyberdefences in place. Building up such cyberdefences can be

costly for new and small FinTechs. The Bank's engagement with the industry, including via its regional agency network, shows that these costs and risks are particularly acute for businesses that rely heavily on technology as a core part of their business model.

2. **The UK's payments infrastructure needs to keep pace with innovation to support economic activity**. Seamless and frictionless payments are critical to economic activity. Co-ordinated action and investment is needed to create the next generation of payment infrastructure that drives innovation, supports competition, and ensures security.

Given the complex and evolving nature of the cyber and innovation landscapes, solutions to these impediments will require collaboration between the financial sector and public authorities. Solutions could include: further publication of potential threats from cyberattacks; the production of guidance documents and signposting to support FinTechs looking to build cyber resilience; and approaches such as innovation sandboxes to allow FinTechs to test out new digital business models.

The FPC welcomes the work of the National Cyber Security Centre to provide advice and guidance on cyber security for SMEs, particularly through its **Cyber Action Toolkit**. The FPC also welcomes the work of the Cross Market Operational Resilience Group to develop solutions and share knowledge within the financial sector. **The FPC judges that there would be benefits in public and industry bodies broadening support to new and small FinTechs looking to build cyber resilience via the provision of targeted advice and guidance.**

The Bank is working with the other UK authorities to deliver innovation in money and payments through supporting HMG's National Payments Vision, chairing the newly established **Retail Payments Infrastructure Board** and expanding the capabilities of our Real-Time Gross Settlement (RT2) service. The Bank is working with industry to deliver practical advancements in the UK's payments infrastructure through the **Synchronisation Lab**, the **Digital Pound Lab** and its **DLT Innovation Challenge**. The Bank's work under the National Payments Vision includes facilitating the development and adoption of tokenised deposits and regulated stablecoins. The FPC welcomes work by the Bank and the FCA to develop a regulatory regime for stablecoins (Section 7).

Tokenised deposits offer the advantages of DLT as well as the benefits of traditional cash such as the deposit insurance provided by the Financial Services Compensation Scheme, providing customers with protection in the event of a bank insolvency. Tokenised deposits could deliver the benefits of programmability and instantaneous settlement, using a product with which customers are already familiar, whilst also being packaged up with credit provision as per the traditional banking model.

> **The FPC remains committed to identifying further ways in which it can deliver on its objectives to support sustainable economic growth.**

The FPC has identified opportunities for the UK financial services sector to further support sustainable economic growth, and barriers to doing so. Public authorities have a key role to play in working with businesses to identify solutions to these impediments. The FPC supports:

- The changes made by the PRA to Solvency II to encourage investment in productive assets by UK insurers, particularly through its reforms to the MA regime and its introduction of a MAIA. This should support delivery of the UK insurance industry's commitment to invest £100 billion in UK productive assets over 10 years.
- Work to ease impediments to high-growth firms accessing funding, including use of public-private partnership funding initiatives to channel financing to these firms and the broader population of SMEs to support productivity improvements, and supporting the working group on lending backed by IP established as part of HMG's Industrial Strategy.
- Efforts by authorities and industry to support the UK financial system's adoption of innovative technology, including through the National Payments Vision, the Bank's AI Consortium and the FCA's AI Lab's Live Testing service.

In line with the FPC's remit letter, published alongside the Autumn Budget 2025, the Bank will continue to build on this work, including by monitoring the progress against issues identified and identifying further actions that could support the supply of long-term productive finance.

The Bank will continue to deliver and support research on growth and the financial system as part of its **Bank of England Agenda for Research, 2025-2028**.

Box B: Evolution of lending in the UK economy

This box describes the evolution of the supply of credit to UK households and non-financial corporates, including small and medium-sized enterprises (SMEs), following the financial market liberalisation reforms in 1986.

This covers four distinct periods: (1) the build-up to, and recovery from, the early 1990s credit-fuelled boom and recession; (2) an unsustainable build-up of debt ahead of the financial crisis; (3) deleveraging over 2009–14 as borrowers and the banking system derisked their balance sheets, while non-bank credit to corporates continued to increase; and (4) since 2014, a recovery in bank credit supply that has proven resilient through a series of shocks. Throughout these periods, SMEs have faced historical access to credit challenges reflecting both supply and demand effects.

UK bank lending in the 1980s and early 1990s grew rapidly as deregulation led to an expansion beyond traditional business lending, which increased the banking sector's size but created vulnerabilities.

The 1980s and early 1990s marked a structural shift in the UK banking sector driven by deregulation and increased competition. The removal of credit controls, exchange restrictions, and reforms such as the abolition of the 'corset' in 1980, enabled banks to expand beyond business lending into mortgage finance and investment banking.[4] Banks' share of mortgage lending increased as a result. Rapid credit growth and loosening of underwriting standards during this period increased vulnerabilities that resulted in the early **1990s small banks' crisis**.

In aggregate, household and non-financial corporate debt doubled relative to GDP during the 1980s. Between 1985 and 1989 residential property prices increased by nearly 80% and commercial real estate (CRE) prices by almost 90%. The early 1990s recession led to many repossessions, business failures – especially among SMEs – and high impairment rates on banks' lending. The **aftermath of the recession saw a reduction in the reliance of SMEs on bank financing**, with the proportion of small businesses seeking external finance falling from 65% between 1987–90, to around 40% between 1995–97. The corporate sector deleveraged a little after the recession. Household debt was stable throughout much of the 1990s between 60%–65% of GDP, reflecting the subdued housing market that followed the 1990s recession as rates rose and house prices fell (Chart A).

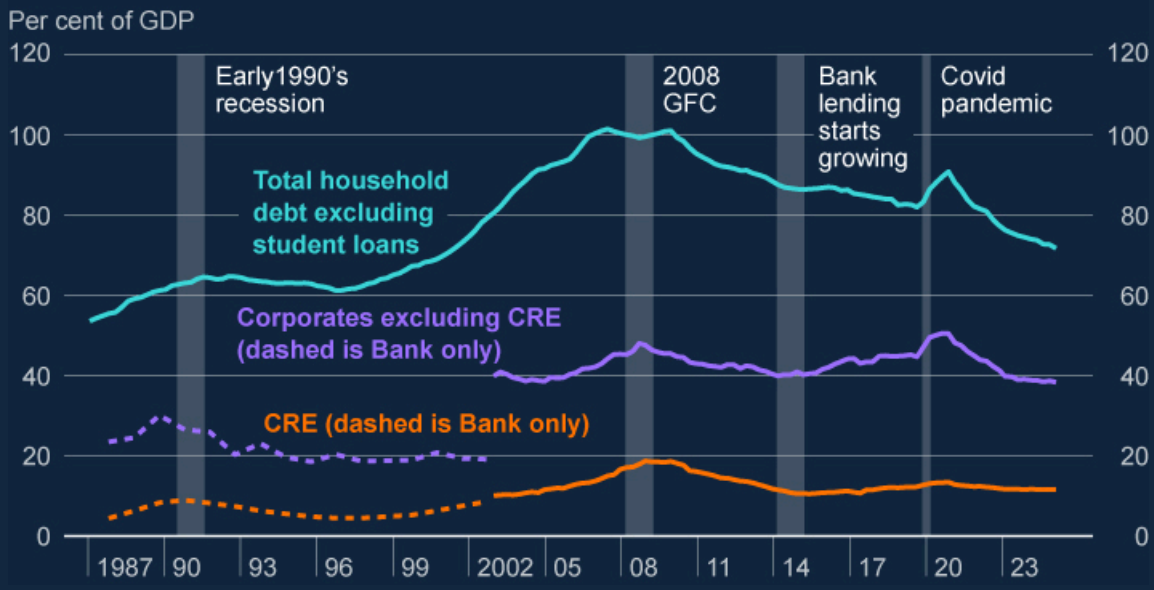
Household and corporate borrowing accelerated in the lead-up to the 2008–09 global financial crisis (GFC) resulting in over-leveraged bank and private sector balance sheets.

Borrowing in the lead up to the GFC proved unsustainable and created vulnerabilities in both the banking sector and the economy that amplified the impact of the financial crisis. Household debt-to-GDP grew by around 40 percentage points from the late 1990's to 2008

and peaked at over 100% of GDP, mirroring rapid house price growth partly driven by increased competition among mortgage lenders (Chart A). Corporate debt-to-GDP rose by less, from around 40% of GDP in 2003 to around 50% by end-2008 though the stock of CRE lending to GDP almost doubled between 2003 and early 2009.

Chart A: Household and corporate indebtedness has fluctuated due to changes in financial and macroeconomic conditions

Total household debt excluding student loans, corporate debt excluding CRE, (a) and CRE debt (b)



Sources: Association of British Insurers, Bank of England, Bayes CRE Lending Report (Bayes Business School (formerly Cass)), Deloitte, Finance & Leasing Association, firm public disclosures, Integer Advisors estimates, LCD an offering of Pitchbook, London Stock Exchange, LSEG Eikon, ONS, Peer-to-Peer Finance Association and Bank calculations.

(a) These data are for private non-financial corporations (PNFCs), which exclude public, financial and unincorporated businesses.
(b) CRE is assumed to be lending for the buying, selling and renting of real estate, and the development of buildings.

Lenders and borrowers deleveraged after the GFC until around 2014 as they derisked their balance sheets, while the supply of credit to corporates diversified.

Banks amplified the recession after the GFC by deleveraging and restricting credit that deepened the downturn and slowed recovery. Macroprudential policies, which strengthened the resilience and reduced excessive risk-taking across the financial system, were introduced after the GFC to reduce this procyclical behaviour.

Household credit growth slowed after the GFC as banks tightened lending standards and focused on repairing their balance sheets. The flat total household debt stock meant it declined relative to GDP, falling to below 90% in 2014. Corporates deleveraged with non-

CRE and CRE debt-to-GDP bottoming out in 2014 and 2015 respectively, around their 2004 levels (Chart A). A shift in the provision of corporate finance occurred during this time as the share of market-based debt rose from a pre-GFC average of 43% (2003–07) to over 55% by 2015 (Chart B). This signalled a structural shift in corporate financing that has moved the UK closer to the US, although non-banks still supply relatively less corporate debt to UK firms than their US peers.

> **Following the implementation of post-crisis regulation and policies to increase banking sector competition, bank lending and the stock of household and corporate credit rose between 2014 and 2020.**

Bank lending to households remained subdued in the years after the GFC and lending to corporates began to rise from 2014. This followed the implementation of post-crisis regulatory reforms, including higher capital and liquidity requirements that strengthened and increased confidence in the banking system. Government and regulatory policies designed to increase banking sector competition also increased the number of providers of finance available to household and corporate borrowers.

The stock of credit to households and corporates increased by over 20% from 2014 to end-2019, from around £2.45 trillion to over £3 trillion. The rise in debt was broadly in line with economic growth in nominal terms, which had slowed from a pre-GFC average four-quarter growth rate of 5% to below 4% between 2014 and end-2019. Therefore, the aggregate household and corporate debt-to-GDP ratio was broadly stable over the period, although this masked a slight increase in the corporate debt-to-GDP ratio offset by a slight decline in the household debt ratio.

> **The economy was hit by a series of shocks starting in 2020 that ultimately resulted in high inflation driving a marked reduction in household and corporate debt-to-GDP ratios, while post-GFC regulation has enabled the banking system to weather shocks while supporting the economy.**

The stock of corporate debt rose by 6% over 2020 H1 as many businesses, especially SMEs, faced severe cash flow issues due to lockdowns and reduced consumer demand. This led to a surge in demand for emergency finance, including government-backed loans. This, combined with a roughly 16% contraction in nominal GDP during lockdown, resulted in large increase in household and corporate debt-to-GDP ratios. This reversed as the economy reopened following the Covid pandemic.

Following this, a series of energy and supply shocks that increased inflation and nominal GDP resulted in a large reduction in debt-to-GDP ratios. The overlapping effects of these shocks, which resulted in interest rates increases, have created a prolonged period of uncertainty, making businesses more cautious about borrowing for expansion. While corporate and household debt increased over this period, by over £100 billion and £200 billion respectively between 2020 H1 and now, this increase was far lower than the near

£800 billion increase in nominal GDP over this period. The reduction in indebtedness of households and corporates relative to their income has led to an increase in resilience to future shocks (Section 3).

Post-GFC regulation that increased bank resilience and the **FPC's use of the countercyclical capital buffer in stress**, has enabled the banking sector to continue to support households and businesses through recent shocks. More recently there are signs that lending growth has picked up (Chart A), which should support household consumption and business investment.

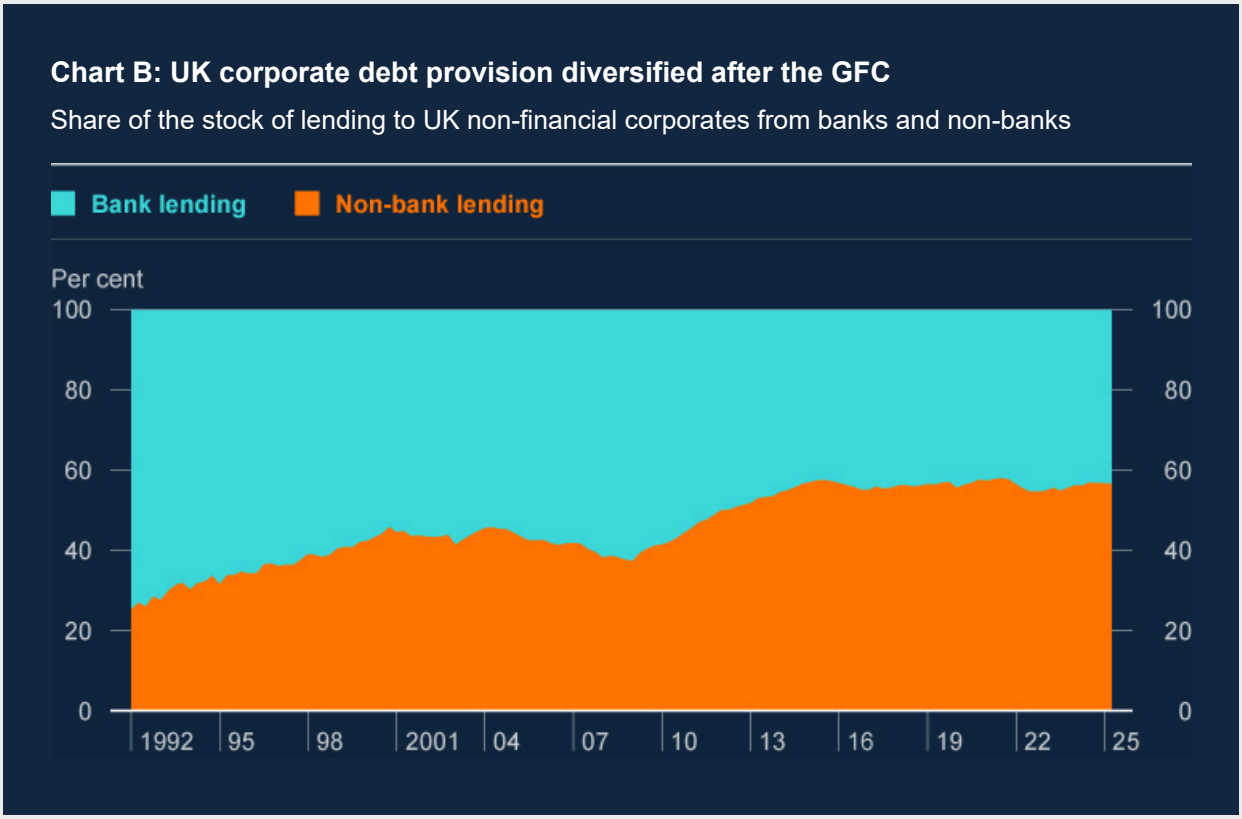
> **In aggregate, bank lending remains a dominant source of direct lending to households and corporates, although large corporates in particular diversified in the years following the GFC.**

Bank lending accounts for the vast majority of household and SME borrowing, and a significant portion of large corporate loans. Large corporates in particular led the diversification of corporate funding after the GFC, although the share of non-bank provided credit has then remained broadly steady over the past decade at over 55% (Chart B). Banks also provide liquidity insurance in the form of undrawn facilities to corporates that can be used in stress. These total around £250 billion in the most recent data for UK banks.

The increased diversification of UK corporate finance has been further increased by international banks and by the emergence of challenger banks. The former have increased their share of bank lending to UK corporates from 17% in the years before the GFC to 27% today. Challenger banks have also increased their share of corporate lending. A number of these challengers make innovative use of big data, in part provided by government initiatives such as Commercial Credit Data Sharing, which enables them to replicate some of the benefits of the relationship banking model, without the need for an extensive branch network.

Chart B: UK corporate debt provision diversified after the GFC

Share of the stock of lending to UK non-financial corporates from banks and non-banks



Source: Refer to the sources for Chart A.

Borrowing by SMEs has fallen as a share of GDP since the GFC reflecting both supply and demand effects, and historical access to credit challenges.

The stock of SME debt as a share of UK GDP has fallen over the past 15 years, from 13% in 2011 Q4 to 8% in 2024 Q4 (Chart C) despite the growth of challenger banks. This reflects both the small share of SMEs seeking external finance and historical barriers these firms face in accessing external financing. These barriers are not unique to the UK, with SMEs across many economies facing similar challenges.

Identifying whether SMEs face a supply-side constraint or a lack of demand for finance is difficult. For example, **Bank of England survey evidence** suggests that many SMEs do not intend to expand their business and so do not need external finance for growth, and around 70% would prefer slower growth over taking on debt. However, concerns around a structural funding gap are not new – the issue has been formally recognised since at least the **Macmillan Committee Report (1931)**. While financing is just one of many factors that influence the growth of a SME, the persistence of these concerns over nearly a century suggests that access to finance for SMEs still suffers from frictions.

Chart C: Total SME debt has been declining as a share of GDP for much of the past 15 years

Aggregate SME gross debt to GDP (a)

Sources: Bank of England, ONS, Peer-to-Peer Finance Association and Bank calculations.

(a) Includes private and public businesses so not fully comparable to aggregate PNFC stats. Data starts in 2011 Q2.

The latest intelligence from the Bank's agents suggests that credit conditions for SMEs have returned to normal, but that many SMEs remain deterred from borrowing. High cost and difficulty accessing sources of finance are two of the most cited barriers. The high cost, relative to lending to larger corporates, can be mostly attributed to higher impairments (through higher probability of default) and operational costs of SME lending (eg small loan size, and high screening costs due to information asymmetries).

> **Actions by the Prudential Regulation Authority (PRA), public authorities and the government should also support the supply of credit to SMEs, and complement work the FPC is undertaking to identify and suggest actions to improve the flow of finance to high-growth-firms (Box A).**

The PRA will apply a Pillar 2A lending adjustment to ensure that the removal of the SME support factors under Pillar 1 do not cause an increase in overall capital requirements for SME lending under Basel 3.1. Likewise, the **updated minimum requirement for own funds and eligible liabilities** (MREL) policy means smaller lenders, covering many of those that are increasing lending to SMEs, will use a 'modified insolvency' strategy, that should reduce unnecessary complexity and cost for these firms and free up capital that can be used to support lending. The PRA is also currently working with HM Treasury to explore how the ring-fencing regime could be further reformed to allow ring-fenced banks to support SME scale-ups, with a report due to be published in early 2026. Government actions, such

as the consultation on **Commercial Credit Data Sharing**, and other actions mentioned in Box A like the launch of the Government's **Business Growth Service**, should further improve the ability of the financial sector to provide finance to SMEs.

2: Developments in global vulnerabilities and financial markets

2.1: Developments in the global risk environment and financial markets

Risks to financial stability have increased during 2025. Global risks remain elevated and material uncertainty in the global macroeconomic outlook persists. Key sources of risk include geopolitical tensions, fragmentation of trade and financial markets, and pressures on sovereign debt markets. A crystallisation of such global risks could have a material impact on the UK as an open economy and global financial centre.

Geopolitical risk remains high. Trade policy uncertainty has remained elevated with the escalation and subsequent de-escalation around China's rare-earth export controls, and the US Supreme Court is currently hearing a case on the legality of tariffs imposed by the current US administration. This uncertainty persists even though, since the July FSR, there have been announcements of a number of bilateral trade deals between the US and partners. In addition, new sanctions imposed on Russian oil over their continued war in Ukraine are a potential source of volatility in the oil market. Elevated geopolitical tensions increase the likelihood of cyberattacks and other operational disruptions, discussed in more detail in Section 7.

Tariffs are expected to weigh on global growth, driven both by the direct impact of tariff barriers and the dampening effect of trade policy uncertainty on firms' investment decisions. Analysis in the **November 2025 Monetary Policy Report** found that tariffs were having a relatively limited effect on global growth to date, but it is too early to judge whether this reflects diminished or merely delayed effects of trade policy changes.

Respondents to the Bank's latest **Systemic Risk Survey - 2025 H2**, covering a range of financial institutions, cited geopolitical risk as the second largest systemic threat to the UK financial system, behind cyberattacks.

Against this uncertain backdrop, the appropriateness of financial regulation is being debated actively across a number of jurisdictions. Robust regulatory standards and international co-operation are necessary to maintain the resilience of the global financial system, limit regulatory arbitrage, and to prevent and respond to shocks in order to support sustainable economic growth over the long term.

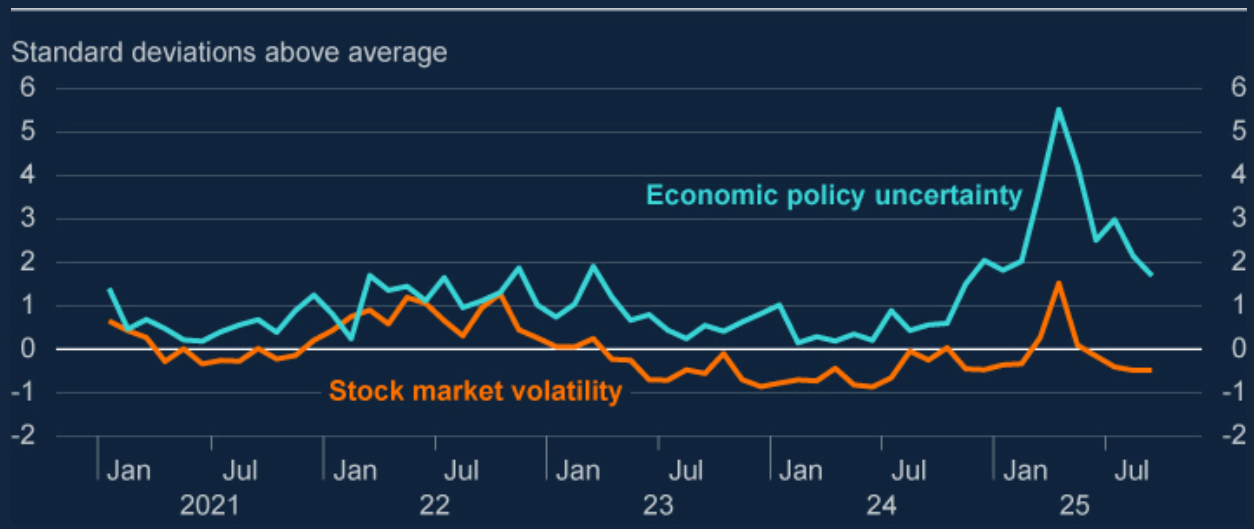
In the FPC's judgement, many risky asset valuations remain materially stretched. This heightens the risk of a sharp correction.

Stock market volatility has fallen since April, and has recently been below its long-term average. Some risky asset prices across advanced economy corporate bond and equity markets have increased since the July FSR, and risk premia across many risky asset classes remain

compressed by historical levels, although have widened somewhat relative to the FPC's October meeting. Economic policy uncertainty remains high, although it has fallen from the levels seen in April (Chart 2.1).

Chart 2.1: Stock market volatility has fallen while economic policy uncertainty remains high, even though it has fallen since April

Standard deviations above the historical average of the Economic Policy Uncertainty Index and Cboe Volatility Index (a) (b) (c)



Sources: Cboe Volatility Index (VIX), Economic Policy Uncertainty Index and Bank calculations.

(a) The Economic Policy Uncertainty Index is a news-based measure of policy uncertainty in 18 countries.
(b) The VIX is an index of US equity market volatility derived from the prices of S&P 500 index options expiring inside 30 days.
(c) Data to the end of September.

Markets do not appear to be fully reflecting the persistent material uncertainty in the global economic and policy environment, and the potential for adverse outcomes. Some risks are difficult to price, either because they are very unlikely to occur or their impacts are highly unpredictable. The risk of a sharp correction remains high. If participants were to reassess their outlook abruptly this could cause asset prices to realign to the prevailing high level of uncertainty.

The risk of a sharp correction sits against a backdrop of rising public debt-to-GDP ratios in many advanced economies, potentially constraining their governments' capacity to respond to future shocks. Significant shocks to the global economic or fiscal outlook, should they materialise, could be amplified by vulnerabilities in market-based finance (MBF), such as leveraged positions in sovereign debt markets.

> **Notably, equity market valuations for technology companies focused on artificial intelligence (AI) remain materially stretched. On some measures, equity valuations are close to levels not seen since the dot-com bubble in the US, and the global financial crisis**

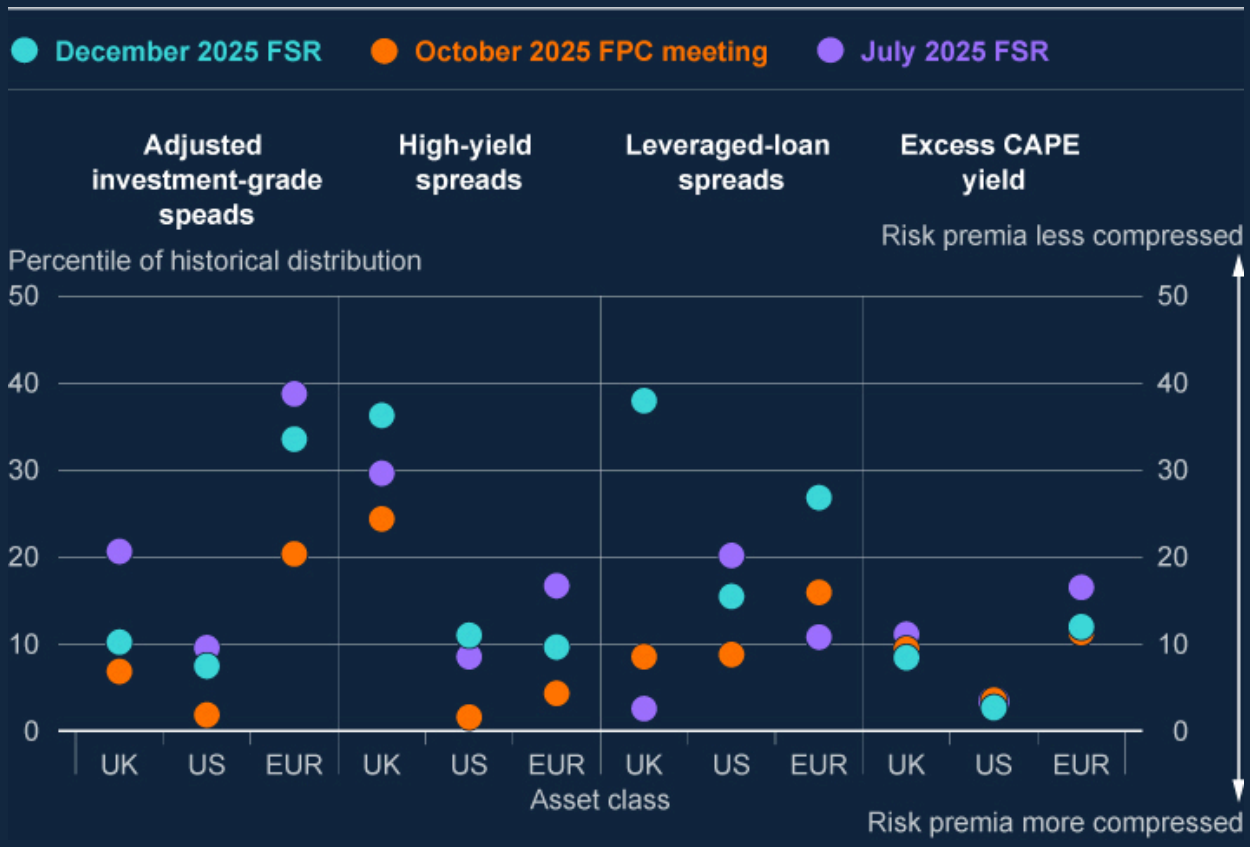
in the UK.

Equity indices, including the FTSE 100 index and S&P 500 index, reached all-time highs in the second half of this year. Equity valuations on some measures (for example the excess cyclically-adjusted price-to-earnings (CAPE) yield) look stretched relative to historical levels across jurisdictions, especially in the US where, on some measures, they are close to levels not seen since the dot-com bubble (Chart 2.2). On a three year forward basis – ie accounting for projected earnings growth over the next three years – excess earnings yield over inflation-protected government bonds in the US is also close to levels not seen since the dot-com bubble.

The equity prices of some large US technology companies focused on AI have continued to increase since the July FSR, although have fallen in recent weeks. The size of these companies has increased concentration in the S&P 500 index to historical highs, with the ‘Magnificent 7’ accounting for over a third of the index.[5]

Chart 2.2: Valuations for a range of risky assets remain at historically stretched levels

Current levels of selected risk premia as a percentile of their historical distribution, compared to levels at the July 2025 FSR and October 2025 FPC meeting (a)



Sources: Bloomberg Finance L.P., Datastream from LSEG, ICE BofAML, PitchBook Data, Inc. and Bank calculations.

(a) Risk premia data are a percentile of a three-day rolling average (except for leveraged-loan (LL) spreads, which are a percentile of a monthly average). Percentiles are calculated from 1998 for investment-grade spreads and high-yield bond spreads, from 2008 for LL spreads and from 2006 for excess CAPE yields. Data updated to 24 November 2025 apart from LL which is to 14 November 2025. Investment-grade spreads are adjusted for changes in credit quality and duration. All data are daily except for LL spreads which are weekly.

Some of these firms are trading at price-multiples that imply high levels of future earnings growth. Whether these earnings will be realised, or even prove underestimates, is uncertain. These prices are exposed to a sharp correction if the prospects for AI development, or for the companies to monetise and generate profits from the use of AI, are revised. Given the concentration of the market, investors exposed to the aggregate index will face a high level of pass through from any sharp correction in AI-focused firms.

The role of debt financing in the AI sector is increasing quickly as AI-focused firms seek large-scale infrastructure investment. By some industry estimates, AI infrastructure spending over the next five years could exceed $5 trillion US dollars. While very large technology companies (widely referred to as the ‘hyperscalers’) will continue to fund much of this from their operating cash flows,

approximately half is expected to be financed externally, mostly through debt. Deeper links between AI firms and credit markets, and increasing interconnections between those firms, mean that, should an asset price correction occur, losses on lending could increase financial stability risks. This is discussed in more detail in Box C.

Corporate credit spreads remain compressed by historical standards, despite continuing macroeconomic uncertainty, including over the impact of higher tariffs on the corporate sector across major economies.

The spread between yields on both investment grade (IG) and riskier corporate borrowing (high-yield bonds and leveraged loans) and yields on safer debt (eg government bonds) have widened marginally since the FPC's October 2025 meeting across jurisdictions, partly as a response to some high-profile US corporate defaults. However, the level of spreads remains tight by historical standards, especially in the US.

The tight level of spreads contrasts with potentially growing vulnerabilities among corporates in a variety of sectors across advanced economies. Corporates, especially highly leveraged corporates, continue to face challenges as they refinance existing fixed-term debt at higher rates following increases in interest rates over recent years (Section 3). However, tight credit spreads have offset this in part and encouraged higher levels of corporate issuance. Higher debt servicing burdens could put pressure on corporate balance sheets and debt affordability.

In addition, tariffs pose specific challenges for exposed corporate sectors in affected jurisdictions. The imposition of tariffs could potentially lead to lower profits for firms through higher costs on imported goods and lower earnings – through either lower global demand, or in response to higher prices if firms pass the cost of tariffs onto consumers. Sectors that are import and export oriented, such as manufacturing (and car manufacturing specifically) and retail and wholesale trade, are likely to be most exposed to this risk. The impact of tariffs on global growth appears to have been limited to date but it is too early to judge whether this reflects diminished or merely delayed effects of trade policy changes.

In response to two recent high-profile corporate defaults in the US, credit spreads widened slightly but have not materially repriced, suggesting market participants primarily see them as driven by company specific-challenges.

First Brands Group, a major automotive parts supplier, and Tricolor, a provider of loans to subprime borrowers for car purchases, both failed in September. Credit markets have not responded materially to these events: spreads remain tight historically for IG and riskier borrowers in high-yield bond and leveraged loan markets, especially in the US, although spreads for CCC ('junk') rated debt have widened relative to other borrowers. This suggests markets broadly see these defaults as driven by company-specific challenges. For example, a proportion of First Brands Group's supply chain was located overseas and therefore potentially subject to tariffs, and Tricolor specialised in providing credit to subprime borrowers, a segment characterised by relatively high default rates.

While the impact of these specific defaults has been limited, they have intensified focus on potential weaknesses in riskier credit markets previously flagged by the FPC.

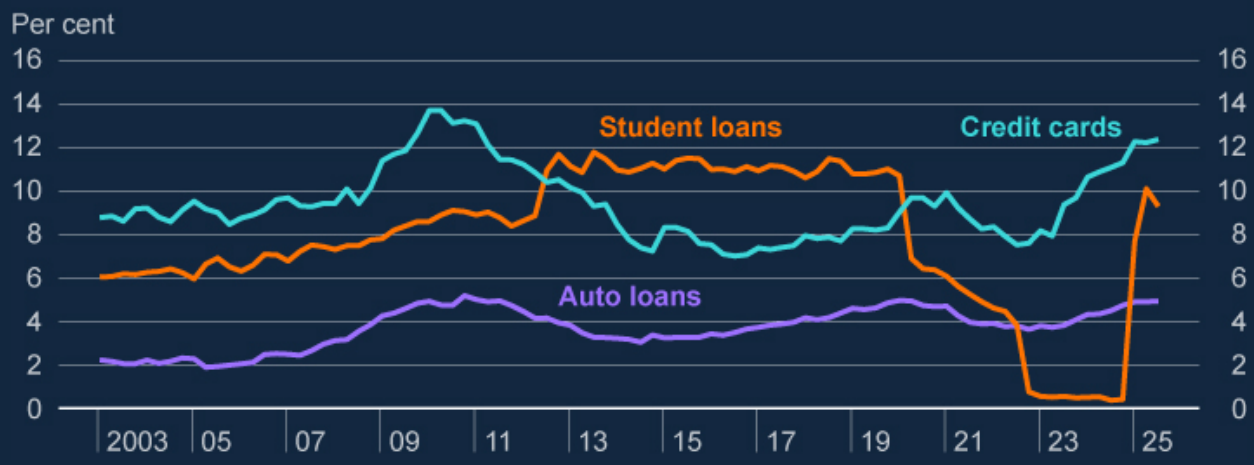
These potential weaknesses in riskier credit markets, such as leveraged loans, collateralised loan obligations and private credit, include high leverage, weak underwriting standards, opacity, complex structures, and the degree of reliance on credit rating agencies. These weaknesses illustrate how corporate defaults could impact bank resilience and credit markets simultaneously.

Further defaults could follow if some of these weaknesses are more widespread. Notably, the opacity and complex corporate structures in these two entities may have been a contributing factor that allowed significant alleged fraud to be undetected for a period. In both of these cases, as well as some other recently disclosed losses, there have been reports that the collateral against which lending was secured was misrepresented or even fraudulent. This could be indicative of weaknesses in underwriting standards.[6] The weaknesses exposed by these defaults is discussed in more detail in Section 6.

These defaults also reflect a potential weakening in credit quality among the lower end of the US income distribution. Subprime auto loans, such as those originated by Tricolor, are typically among the first asset classes to experience distress in a deteriorating macroeconomic environment. The US consumer appears resilient in aggregate – the proportion of mortgages in arrears remains relatively low by historical standards and household debt-to-GDP has continued to fall – but there are vulnerabilities among households at the lower end of the income distribution. 90+ day arrear rates on different forms of US consumer credit have increased markedly over the past three years (Chart 2.3).

Chart 2.3: 90+ day arrear rates on different forms of consumer credit in the US have increased

Proportion of balances at least 90+ days in arrears on different forms of US consumer credit (a)



Sources: Equifax and Federal Reserve Bank of New York.

(a) Arrears on student loan debt increased significantly in the first half of 2025, reflecting the resumption of student loan repayments and reporting of delinquent loans to credit bureaus.

Weakening credit quality is especially prevalent in subprime auto loans, such as those provided by Tricolor. The arrears rate on auto loans by subprime borrowers that have been securitised in asset-backed securities (ABS) has increased sharply over the past few years (Chart 2.4).

Chart 2.4: Share of subprime auto ABS loan balances 60+ days in arrears has risen sharply

Proportion of balance on prime and subprime auto loans that have been securitised in an ABS at least 60-days delinquent

Source: Fitch Ratings Research & Data.

US businesses are facing cost pressures due to the imposition of tariffs, especially in exposed sectors. Bank staff analysis suggests the tariff cost shock is relatively small as a share of total corporate profits across sectors, but represents a significant share of profits in more heavily impacted sectors, particularly within manufacturing.

Default rates on speculative grade debt (leveraged loans and high-yield bonds) in the US have increased and are above pre-Covid levels, but have been broadly stable over the past two years (Chart 2.5).

Chart 2.5: Defaults among riskier corporates have increased in the US

12-month average default rate on speculative grade (high-yield bonds and leveraged loans) borrowing in the US and EU

Source: Moody's Ratings.

With sections of the US corporate sector and households facing challenges, further defaults could follow, especially if the economy weakened. If this triggered a wider reassessment of credit quality by global markets, this could lead to higher borrowing costs for UK households and businesses, and lower liquidity in UK corporate bond and leveraged loan markets.

> **The FPC will continue to monitor these issues, and any potential spillovers to the UK. The Tricolor and First Brands defaults reinforce the need for market participants to have a clear understanding of their exposures and ensure that underwriting standards are robust.**

While the impact of – and UK banks' direct and indirect exposures to – these specific defaults has been limited, a diverse range of financial market participants were exposed. Such diversity can help absorb risks, but opacity around the extent of exposures, and their possible interconnections, can also create uncertainty about how widely shocks in credit markets can propagate. It is important that market participants have a clear understanding of their exposures, including in stress scenarios where correlations and losses can shift outside historical norms. Market participants should also ensure that underwriting standards are robust and that they do not over-rely on credit ratings as a substitute to carrying out appropriate due diligence.

If the defaults of First Brands and Tricolor prompted a wider reassessment of credit risk in the US, then this could spillover to the UK and harm the availability and pricing of credit for the UK real economy, with higher spreads and a tightening of credit conditions for lower quality credit in particular.

While the risk of a spillover exists, the FPC judges the UK household and corporate sectors remain resilient in aggregate. Measures of household and corporate indebtedness remain significantly below pre-Covid levels, consumer credit debt servicing ratios remain low, and the share of consumer credit loans in arrears has remained largely stable. Lending spreads in the UK, although still relatively compressed by historical standards, are less compressed than in the US. However, there are pockets of risk among some households, SMEs, and highly leveraged corporates. The resilience of the UK household and corporate sectors is discussed in Section 4.

2.2: Global public sector debt vulnerabilities

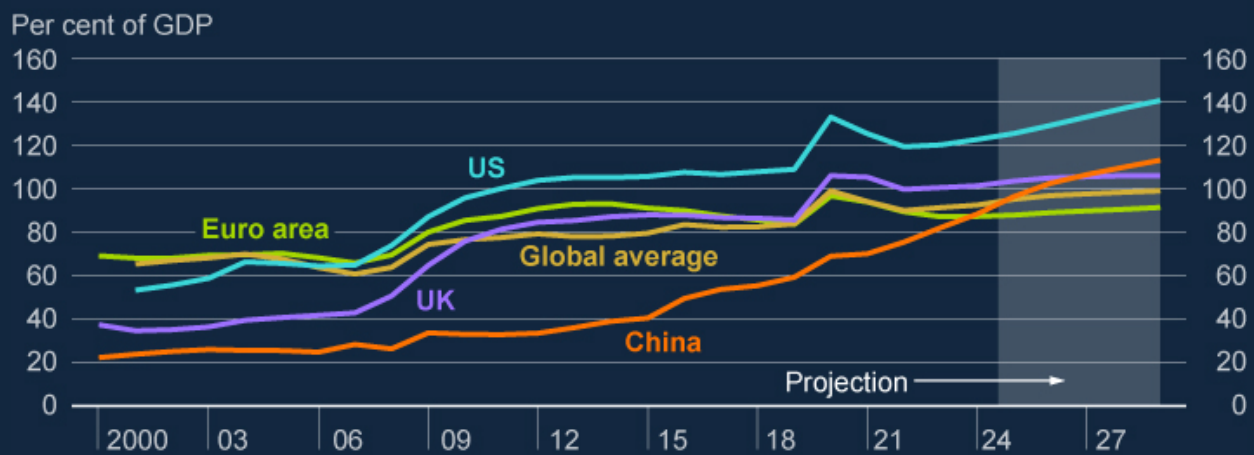
Public debt-to-GDP ratios in many advanced economies have continued to rise this year.

There has been a long-term upward trajectory in public debt-to-GDP ratios across advanced economies in recent decades and significant further increases are expected for some economies in coming years (Chart 2.6).

Governments globally face spending pressures, given the context of changing demographics and geopolitical risk, potentially constraining their capacity to respond to future shocks. Significant shocks to the global economic or fiscal outlook, should they materialise, could be amplified by vulnerabilities in MBF, such as leveraged positions in sovereign debt markets.

Chart 2.6: Debt-to-GDP ratios are projected to continue to increase

Sovereign debt (percentage of GDP) (a)



Sources: International Monetary Fund (IMF) and Workspace from LSEG.

(a) Use of IMF Content and Data is subject to the IMF's terms of Copyright and Usage.

Some countries have faced political uncertainty and change over the level and pace of reforms to improve fiscal outlooks.

France is experiencing challenges agreeing its 2026 Budget. Japan's incoming administration has announced it intends to introduce additional fiscal spending and will target an overall debt-to-GDP ratio, rather than the budget deficit.

The IMF projects that public debt-to-GDP in China is on an upward trajectory. The IMF's broader measure of China's government debt which captures some off-balance sheet debt, such as that held by local governments and associated with their funding vehicles, is forecast to rise to 153% of GDP by 2030. Support for local government finances was announced last November, which brings some local government debts onto balance sheets and reduces financing costs, but local government fiscal pressures remain elevated amidst weak revenue growth. These reforms may act to reduce fiscal space in China, potentially reducing the Chinese government's ability to respond to an economic slowdown.

Continuing adjustment to the property market slowdown and potential economic headwinds from tariffs could drag on the Chinese economy in the coming years. In mainland China the pace of the decline in house prices has increased in recent months, following a stimulus-driven moderation at the start of the year. Given the size and globally interconnected nature of the Chinese economy, this could have potential adverse impacts on global trade and growth and financial markets.

> **Yields on developed market long-term government bonds have risen over recent years reflecting interest rate increases and higher term-premia, as concerns about the sustainability of fiscal deficits globally remain in focus.**

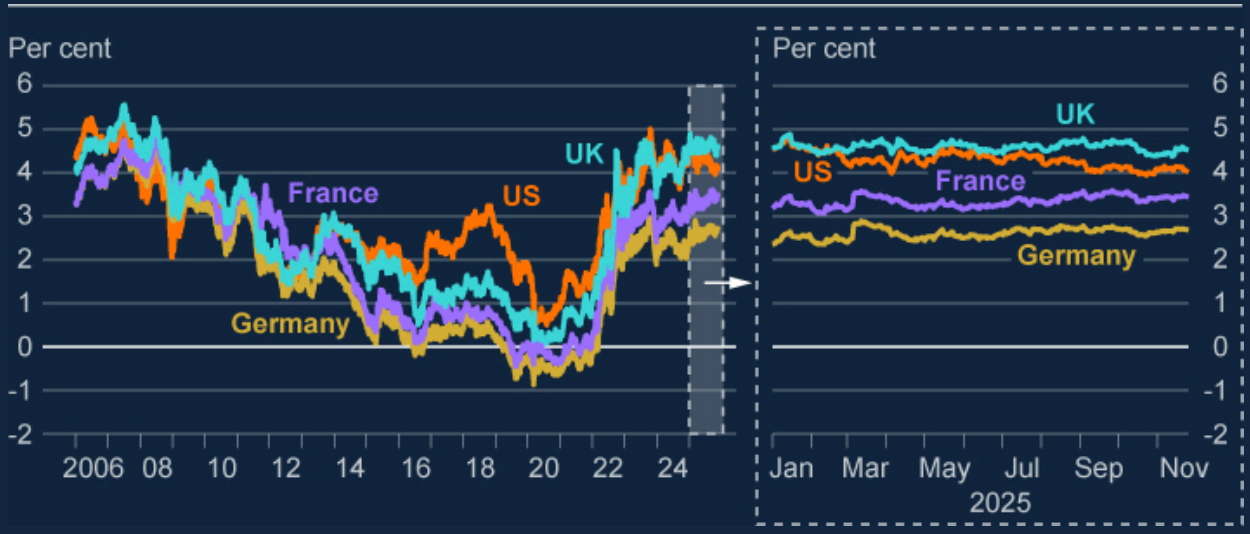
Long-term yields remain elevated relative to recent history (Chart 2.7). This reflects both the increase in interest rates seen across economies since the pandemic and increases in term premia as investors demand a greater premium for holding bonds with longer-term maturities.

Market participants attribute these shifts in global term premia to a combination of factors, including evolving supply and demand dynamics for longer-dated government securities and heightened market scrutiny of the long-term sustainability of fiscal positions.

Since the July FSR, however, yields on 10-year government bonds across jurisdictions have not moved materially. UK 10-year government bond yields initially rose, reaching 4.71% at the time of the FPC's October meeting, before subsequently declining to 4.54%, close to their July level. This fall reflects both reduced term premia and expectations for interest rates. Yields on US 10-year government bonds exhibited a similar trajectory and now sit below their July levels. 10-year government bond yields in France and Germany are also around their level at the time of the July FSR.

Chart 2.7: Long-term (10-year) government bond yields have risen over recent years reflecting interest rate increases and higher term-premia.

US, UK, French and German 10-year government bond yields (a)



Source: Bloomberg Finance L.P.

(a) Data as at 24 November 2025.

There are a number of channels through which pressure on sovereign debt could impact UK financial stability.

As explored in the **November 2024 Financial Stability Report**, there are a number of channels through which pressures on sovereign debt globally could affect UK financial stability. These include: increased market volatility and possible interactions with vulnerabilities in MBF; the reduced ability of governments to respond to future shocks; higher interest rates leading to tighter global financial conditions; and the potential for capital outflows from non-resident investors.

As an open economy with a large financial centre the UK is exposed to global shocks, which could transmit through multiple, interconnected channels. Stress in one market, such as a sharp asset price correction or correlation shift, could spillover into other markets. Simultaneous derisking by banks and non-banks can lead to fire sales, widening spreads and tightening financing conditions for UK households and corporates. Market participants should ensure their risk management incorporates such scenarios.

A number of jurisdictions are seeing a longer-term shift in the composition of buyers for their sovereign debt. Historically, pension funds have been large buyers of longer-term government bonds, but have played less of a role in recent years as higher interest rates improve their funding ratios, and an ageing population may encourage funds to shift toward shorter-term assets to ensure liquidity for paying current benefits. In contrast, multinational non-bank financial institutions such as hedge funds are playing an increasing role. Hedge funds have had a sizeable presence in

US and UK government bond markets for a number of years. Analysis published in the latest **Bank of Japan Financial System Report** highlighted that the presence of hedge funds engaging in arbitrage trading in the Japanese government bond market appears to be growing.

In normal times, hedge funds serve a useful function by warehousing risk and intermediating between different types of market participants, thereby improving market liquidity and price discovery, but their use of leverage introduces risk. Leveraged market participants employ strategies which can be vulnerable to shifts in financing conditions or increases in margin requirements. This can cause them to reduce risk, potentially amplifying volatility during periods of stress. Correlations between movements in yields across sovereign issuers – in part reflective of the presence of similar investors across different markets – could act to transmit and amplify stress in government bond markets. As an open economy and global financial centre these risks could have a material impact on the UK. The resilience of the UK gilt and gilt repo markets are discussed in Section 6.

Box C: Financial stability risks from the impact of AI development on financial markets

The FPC has previously set out its view that Artificial Intelligence (AI) is likely to have a transformational impact on the UK economy, though the scale and time horizons are uncertain.

Ensuring that the 'AI transition' occurs without compromising the resilience of the financial system is important for delivering sustainable economic growth. Financial stability consequences could arise both in scenarios where AI capabilities and adoption improve quickly or if AI progress does not deliver the returns expected by investors and the companies involved. The FPC published a **Financial Stability in Focus paper** in April 2025 on the opportunities and risks from the use of AI within the financial system. This box focuses on the impact of AI development on financial stability through its consequences for financial markets.

The capabilities of AI systems have continued to improve quickly in the past 18 months. The progress in AI systems and the development of physical infrastructure to train, use and power them has resulted in a wide range of companies across multiple sectors – from technology to utilities and capital goods (referred to as 'AI companies' in this box) – being at least partly dependent on AI progress for their current and expected future earnings.

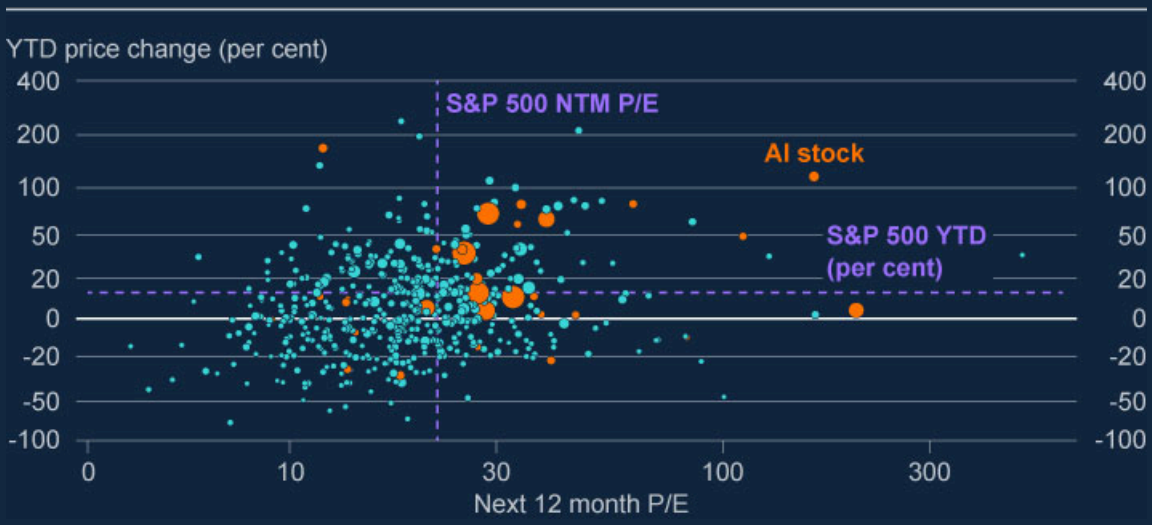
AI developments have been an increasing driver of equity markets in 2025.

AI companies now account for 44% of the market capitalisation (up from 26% in 2022) and 67% of the year-to-date returns of the S&P 500 (which comprises around half of the value of global equities). They also account for a high share of major equity indices in several other countries (eg South Korea and Japan), though the UK's FTSE 100 index is relatively less affected.

The share prices of many AI companies are partly underpinned by high expected future earnings growth over several years, contributing to those companies – and subsequently the equity indices which they comprise a significant part of – appearing historically expensive in valuation metrics which consider past, current or only near-term future earnings (Chart A). The US excess cyclically-adjusted price-to-earnings (CAPE) yield – a measure of equity risk premia (ERP) which considers past earnings – is close to its lowest level since the dot-com bubble. CAPE is a backward-looking measure, but even ERP calculated from the excess yield of three-year forward earnings expectations is at its most compressed level in 20 years. Whether these earnings will be realised, or even prove underestimates, is uncertain.

Chart A: AI stocks have driven the high valuation and growth of the US stock market. These AI company valuations are partly underpinned by the expectation of high future earnings growth

Year-to-date price change of S&P 500 stocks, per cent, and next 12 month price-to-earnings (a) (b) (c)



Sources: Refinitiv Workspace and Bank calculations.

(a) The chart uses a pseudo-log scale with base 10 and a sigma of 20 for visualisation purposes.
(b) The size of dots corresponds to the market capitalisation of firms as of 24 November 2025.
(c) 'AI stocks' are those which appear in the JPAIM equity basket.

AI infrastructure investment has mostly been financed by the cash flows of large, profitable technology companies and equity investments to date.

AI infrastructure investments have to date largely come from a small number of very large technology companies (Microsoft, Alphabet, Amazon and Meta – widely referred to as the 'hyperscalers') with strong balance sheets, who have mostly financed these investments from their operating cash flows. Though there is some sensitivity to underlying assumptions (eg the categories of investment classified as 'AI-related' in national accounts, the assumed import intensity of investment and the use of firms' revenues and capital expenditure in the calculation), Bank staff estimate that in the first half of this year, AI investment accounted for about half of US GDP growth.

However, the financing of AI development is reaching an inflection point and while currently modest, debt financing is increasing quickly across multiple funding channels.

The 75 investment grade (IG) corporate issuers that JP Morgan Research estimate are most closely tied to the AI revolution already account for 14.5% of the **JULI IG corporate bond index** (up from 11.5% in 2020) – a higher share than the largest current sector (US

banks). Within that, the average credit rating for these issuers is high (A-), the AI hyperscalers all have a credit rating of AA- or higher and at present only account for a small share of the outstanding AI IG debt. Most (but not all) AI-related issuers have stable or positive credit outlooks.

However, the second half of 2025 has seen the issuance of a large volume of corporate debt by some AI companies, a proportion of which has been raised through project-finance style off-balance sheet vehicles (eg $27.3 billion of bonds issued by the holding company Beignet Investor LLC to fund Meta's Hyperion Data Centre in Louisiana). The bond market has absorbed this issuance so far – US IG corporate bond spreads remain near their lowest level over the past 15 years. But debt securities and credit derivatives associated with AI companies can quickly reprice in response to changes in outstanding debt volumes and/or future earnings expectations. For example, the five-year credit default swap spreads of Oracle – an AI company which has lower free cash flow margins than some other larger hyperscalers and has issued a large amount of debt this year to finance AI infrastructure spending – has widened from less than 40 basis points to around 120 basis points since end-July (by contrast, the credit default swap spreads of US IG corporates more broadly – as proxied by the CDX North American IG five-year index – are broadly unchanged over the same period).

Using Pitchbook data, Bank staff also estimate that new general lending to AI companies across the leveraged-finance and private market debt universe (comprising term loans, credit facilities and a limited share of bond issuance) increased by a factor of three between 2023 and 2024 and then again further in 2025 to almost $100 billion year-to-date. Both banks and non-banks provide a significant share of this debt, with the biggest lenders being investment banks (who are also important participants in core financial markets) and large investment managers in private markets. Some of this lending is subsequently distributed or packaged into collateralised loan obligation structures, spreading exposures across a wide range of banks and non-bank investors. As a result, tracing the final location of credit risk is challenging, complicating assessments of who ultimately bears losses if conditions deteriorate.

> **This debt financing is expected to increase significantly in the coming years. The buildout of AI infrastructure to train and use AI systems is by some estimates expected to require more than five trillion US dollars of investment over the next five years and a significant but uncertain share of this is likely to be financed by debt.**

The scale of this spending on AI infrastructure is underpinned by the expectation that increasing the computational power dedicated to training AI models will improve their capabilities – known as 'scaling laws' – and that these higher system capabilities will result in large demand for using AI systems. The size of future AI systems necessary for further

scaling combined with the growing demand for using AI underpins the scale of these projected capital investments. AI use (commonly referred to as 'inference') is expected to increase from 30% to 70% of AI data centre capacity by 2029.

While there are a range of estimates across firms, there is broad consensus that AI infrastructure investment will be in the trillions of dollars over the next five years. A significant, but uncertain share of this investment is likely to be financed by debt. For example, Morgan Stanley Research estimate that AI infrastructure spending between 2025 and 2028 will be $2.9 trillion. While hyperscalers are expected to continue to leverage their operating cash flows for a large share of this investment, $1.5 trillion is expected to be met by external capital from a wide range of sources across (mostly) debt and equity, including $800 billion from private credit. JP Morgan expect the same AI IG corporate issuers to account for over 20% of the JULI index by 2030. The expectation of growing debt financing of AI infrastructure investments was noted by multiple firms in recent market intelligence conducted by the Bank.

> **There are a range of developments that could trigger a re-evaluation of future AI company earnings or project revenues and a subsequent fall (or rise) in the price of AI-impacted equities and credit instruments.**

This could include (but is not limited to) an event – for example an AI model release, survey result or AI company earnings announcement – which triggers a re-evaluation of future earnings based on the underwhelming speed of AI capability progress or user adoption of AI, or below-expectation ability of AI companies to monetise the users of their AI applications. It is also possible that these factors could trigger an earnings surprise to the upside – the speed of AI progress and economic impact is highly uncertain, as seen in the wide range of estimates by **AI experts** and **economists**. Other important sources of uncertainty include the degree of physical constraints to rapid AI infrastructure development (most likely access to power), the depreciation lifecycle of AI chips which comprise around half of AI data centre costs, and the society-wide reaction to increasingly transformational AI.

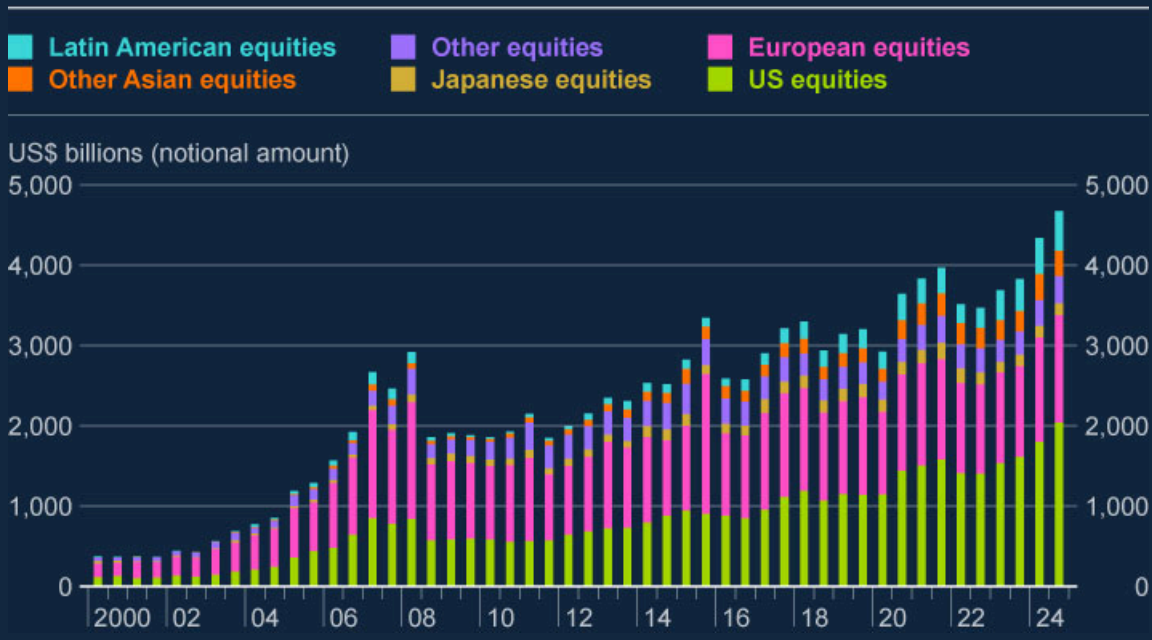
> **The predominantly cash and equity-financed nature of AI development to date limits the likelihood of severe systemic risk implications of a change to AI-driven asset prices in the near term.**

The impact of asset price bubbles on systemic risk depends crucially on which actors are exposed and are greater when vulnerabilities such as leverage and liquidity mismatch exist, which can amplify shocks and impose externalities on the rest of the financial system. In that context, the nature of the AI 'boom' as primarily an equity story up until this year has meant that a fall in AI-related asset prices would not necessarily lead to severe financial stability consequences.

However, the collapse of Archegos Capital Management in March 2021, after failing to meet margin calls on their equity total return swap positions, demonstrated how leveraged equity positions can result in risks to systemic financial institutions through prime brokerage exposures when prices fall. Using UK European Market Infrastructure Regulation trade repository (EMIR-TR) data, Bank staff do not currently observe signs (large exposures from speculative investors spread across multiple dealer counterparties) of dangerous hidden leverage in equity derivatives referencing key AI companies. However, this data only covers transactions involving at least one UK counterparty, so this does not eliminate the possibility that these risks exist. Furthermore, data from the Bank of International Settlements (BIS) shows that the notional outstanding value of global (particularly US) over-the-counter (OTC) equity-linked forwards and swaps has grown consistently over time, and more quickly in recent years (Chart B).

Chart B: The notional outstanding value of equity-linked forwards and swaps have increased quickly in recent years. This is part of a longer-term trend of the equity derivative market growing in size and the share of contracts within that tied to US equities also increasing

Notional value of equity-linked forwards and swaps by market, US$ billions (notional amount) (a)



Sources: BIS and Bank calculations.

(a) 'Equity derivatives' refers to OTC equity swaps and forward contracts.

An AI-driven fall in equity prices would have a greater impact on the US economy, with consequences for the UK through spillovers to broader financial conditions and trade channels.

On top of the contribution of AI investment to US GDP growth, Bank staff estimate that increases in US equity prices have contributed to around 10% of the increase in US real consumption since the start of 2024, with AI-related equities the main driver during this period. The role of equities as a share of US household wealth has increased from 20% to 34% since the global financial crisis, and equity holdings have also increased relative to incomes in that time, although a large portion of this increase is driven by higher wealth households with a lower marginal propensity to consume. A sharp, sustained repricing of equities could have a meaningful impact on US GDP growth through a wealth-effect-driven fall in consumer spending and tighter financial conditions.

UK households would be exposed to a significant AI-driven fall in equity prices through their global holdings of AI-exposed stocks. There could also be broader economic effects, if a significant AI repricing raises uncertainty globally and leads to a deterioration in economic sentiment. UK equities typically co-move with other global equity indices and so could fall in such a scenario even though their direct AI exposure is lower. Any significant fall in equity prices could reduce UK household wealth and subsequently consumption. The direct wealth effects on consumer spending in the UK of an AI-driven fall in equity prices are likely to be comparatively lower than the US due to the significantly smaller role of direct equity holdings as a share of household wealth. However, an AI-driven fall in equity prices which raises uncertainty and leads to a deterioration in economic sentiment could also increase risk premia beyond equity markets, for example in corporate bond markets. If persistent, this could propagate through other financial and credit channels, including raising global and UK banks' cost of wholesale funding, and tightening UK financial conditions.

Any sharp repricing of AI-related equities which weakened US demand could in turn also reduce demand globally. Additionally, weaker US demand could lead to lower US incomes and earnings, putting pressure on the debt servicing burdens of US households and businesses and consequently increasing the defaults and losses on the US exposures of UK lenders. A fall in AI-related asset prices would happen in a significantly different macroeconomic context to the early 2000s, increasing the potential correlation between an AI equity-driven macroeconomic shock and dynamics in core financial markets.

> **If debt financing of AI development increases as projected this decade, the financial stability consequences to the UK economy of any AI-driven fall in asset prices could increase.**

The evolution in the size, quality and terms of banks' direct (and indirect) exposures to AI companies will be important factors in the financial stability consequences of any AI-driven fall in asset prices. As well as their direct lending exposures, systemic banks could be exposed indirectly through exposures to non-bank financial institutions such as private credit firms who are important providers of capital to AI projects. If material credit losses on AI lending were to occur (directly or indirectly), this could have spillovers to broader credit conditions including in the UK. The Bank will explore risks from private markets more

broadly (not focused on AI exposures) through the upcoming System-Wide Exploratory Scenario (Section 6) and is also assessing the risks from private markets to banks through the Bank Capital Stress Test (Box F).

Any AI-driven shock could also have an impact on public credit markets, which many UK companies rely on for raising capital, particularly if the shock was amplified by existing financial system vulnerabilities, such as leverage and liquidity mismatches. While at present the degree of impact on credit markets of a re-evaluation of future AI company earnings would likely be modest, if debt issuance increased significantly, the direct impact would become larger. The scale of projected bond issuance alone may be sufficient to cause a material supply-driven widening of spreads across investment and high-yield markets, with direct consequences for the borrowing costs of corporates who use public markets to raise finance.

> **An AI-driven asset price correction could also impact financial stability through commodity markets, with the probability of such an event likely to increase if AI infrastructure scales and leads to a substantial increase in raw material demand.**

For key commodities required in the development of AI and associated energy infrastructure, such an event could represent a demand shock. Very large shocks to commodity prices can have spillover consequences for systemic institutions, as seen in 2022 when large margin calls in LME Nickel futures markets following unprecedented increases in prices forced a suspension of trading by the central counterparty (CCP) LME Clear.

In the coming years, the scale of AI demand for power could also increase wholesale electricity prices, with possible broader economic implications. The UK government has established the AI Energy council to address the challenges posed by the growing energy demands of AI in the UK. If access to power – for example due to delays connecting new AI data centres to the electricity grid – acts as a bottleneck to the operation of AI data centre projects, it can also weigh on their credit risk and be a trigger for re-evaluating future AI company/project earnings.

> **Finally, a scenario in which AI system capabilities and adoption increase very quickly might have wider consequences.**

Such a scenario would likely have a positive impact on UK and global productivity and economic growth. However, it could also result in adverse consequences for the asset prices of companies who fail to adapt or whose business models become obsolete. Market contacts have noted that while it is too early to say with confidence which firms and sectors would be at most risk, software was among the areas more likely to be disrupted in such a scenario and was also an area of high concentration in private credit and leveraged loan markets. There could also be an impact through lower or shifting employment. These risks remain forward looking but could evolve quickly.

3: UK household and corporate debt vulnerabilities

Financially resilient households and corporates play a key role in supporting economic growth in the UK.

A stable financial system, with resilient households and corporates, is a key factor in supporting sustainable economic growth (Section 1). Household savings and corporate investment help drive productivity growth. And highly indebted households and businesses may cut back sharply on consumption, investment, or employment to make debt repayments, worsening economic downturns. The most indebted can default, leading to losses for lenders.

By stress testing banks to ensure they have sufficient capital to absorb significant losses on their household and corporate loans while continuing to lend (Section 5), and through its policy on high loan to income (LTI) mortgages, the FPC aims to reduce risks to financial stability from UK households and corporates and so support economic growth.

3.1: Overview of UK economic developments

The outlook for UK growth over the coming year is a little stronger than it was at the time of the July FSR but remains subdued.

In the **November Monetary Policy Report** (MPR), annual real UK GDP growth was projected to be marginally stronger on average over the next three years than expected in July but remains subdued. While global trade policies and elevated global uncertainty still weigh on medium-term prospects for growth, the global economy has been more resilient to trade developments than expected. The UK labour market has softened, and UK unemployment has reached 5%, where it was expected to peak in 2025 Q4 – before gradually falling back to 4.7% by 2028 Q4. The growth rate of nominal household incomes was slightly stronger in 2025 Q2 compared to Q1, whereas corporate earnings reduced.

At the time of the November MPR, market pricing implied that Bank Rate was expected to be around 3.5% in a year's time, slightly lower than expected in July. In line with the latest developments in monetary policy and a competitive mortgage market, quoted mortgage rates have continued to decrease. And continuing the trend from July, the growth in mortgage market lending has risen to 3.2% year on year, above the post-global financial crisis (GFC) average of 2.2%. Effective rates on new bank lending to corporates have also decreased, with rates for private non-financial corporates declining 14 basis points from August to September.

3.2: UK household debt vulnerabilities

Measures of indebtedness suggest that UK households remain resilient in aggregate.

Aggregate measures of UK household indebtedness have continued to fall since the **July FSR**. The aggregate debt to income ratio remained low at 132% in 2025 Q2, having fallen to its lowest level since 2002. The share of household income spent on mortgage repayments (debt-servicing ratio (DSR)) was flat at 7.3% in Q2 and is expected to remain around this level over the coming years. Sensitivity analysis by Bank staff shows that it would take a very severe shock to incomes and mortgage spreads for aggregate household DSRs to reach historic peaks (Chart 3.1).

Chart 3.1: It would take a large decrease in incomes and increase in lending spreads for household DSRs to reach GFC peaks

Aggregate household mortgage DSR and staff projections under a central and stressed scenario (a) (b) (c)

Sources: Bank of England, Bloomberg Finance L.P., FCA Product Sales Data, ONS and Bank calculations.

(a) Calculated as mortgage interest payments plus principal repayments as a proportion of nominal household post-tax income. Household income is defined as disposable (post-tax) income adjusted for changes in pension entitlements, which is adjusted to exclude gross operating surplus and the effects of financial intermediation services indirectly measured, and to add back interest paid. Mortgage interest payments before 2000 are adjusted to remove the effect of mortgage interest relief at source.
(b) The illustrative projections to end-2027 use projections for household post-tax income consistent with the November 2025 MPR forecast. Payment increases are projected using market expectations for Bank Rate based on the overnight index swap (OIS) curve as of 24 November 2025 taking into account the distribution of fixed-deal terms from the FCA Product Sales Data and assuming the aggregate mortgage debt to income ratio remains constant.
(c) The stressed projection is designed to illustrate the sensitivity of the aggregate household DSR to severe shocks. It assumes both a cumulative 5% fall in disposable (post-tax) household incomes by the end of 2027 – a little larger than in the GFC – as well as a 300 basis points increase in mortgage spreads, which passes through to mortgage borrowers with a lag. The household income measure is adjusted as in the central projection.

The share of households in arrears or with high debt-servicing burdens remains low by historical standards. Aggregate consumer credit DSRs remain low at around half pre-GFC levels and the share of consumer credit in arrears has remained relatively stable at 1.2% in 2025 Q3. The proportion of all households with high mortgage DSRs (defined as DSRs over 40%) was 1.6% in 2025 Q3. This share is expected to remain well below its pre-GFC peak and slightly above projections at the time of the July FSR.

Consistent with this, the rate of mortgage arrears, which was 0.9% in 2025 Q3, is expected to remain well below its early 1990s and post-GFC peaks. The number of homes repossessed by banks increased this year, reaching around 6,100 homes by the end of 2025 Q3 compared to 4,200 at the end of 2024 Q3, although repossession rates remain very low by historical standards at 0.06% of all loans.

The aggregate household savings to income ratio remains elevated, increasing households' resilience to potential future shocks. However, some groups are more vulnerable to economic shocks than others. Evidence from the NMG survey finds that the gap in median savings to income between outright owners and renters has widened over 2025. While falling rental price inflation is likely to somewhat ease pressures on renters, renters also continue to be more likely to report financial difficulty and insufficient emergency savings. Around 35% of households are renters, so sharp spending cuts or defaults on their financial obligations in the event of economic shocks can pose **financial stability risks**.

> **Borrowing costs have decreased following recent reductions in Bank Rate. But there are still some households that are expected to face higher mortgage payments over the next three years.**

Since interest rates started to rise in 2021 H2, many mortgage accounts have refixed onto higher rates. Previous and expected falls in Bank Rate will lead to decreasing mortgage payments for households on variable rates and for households that are currently fixed above prevailing rates. A third of mortgage accounts (three million households) are expected to see payments decrease in the next three years, similar to expectations at the time of the July FSR.

However, some households are expected to see an increase in mortgage repayments, as the full impact of higher interest rates has not yet passed through to all mortgagors. In total, over the next three years, 43% of mortgage accounts (3.9 million) are expected to refinance onto higher rates. On balance, for the typical owner-occupier mortgagor rolling off a fixed rate in the next two years, their monthly mortgage repayments are projected to increase by £64 (8%), with some households facing much larger increases.

> **Lenders have been adjusting their behaviours following the clarification of the FCA Mortgage Conduct of Business (MCOB) rules and the changes in the FPC recommendation for the loan to income flow limit, but the full impact of these policy changes is still passing through to the mortgage market.**

The FPC has set out a recommendation for a 15% aggregate flow limit on new UK mortgage lending to borrowers with high LTI ratios (at or greater than 4.5). This measure provides insurance against a marked and unsustainable loosening in underwriting standards and a further significant increase in the number of very highly indebted households. In addition to the FPC's LTI flow limit, the Financial Conduct Authority (FCA) also has Responsible Lending rules to protect consumers from unaffordable mortgage debt. While these measures and rules have different objectives, both

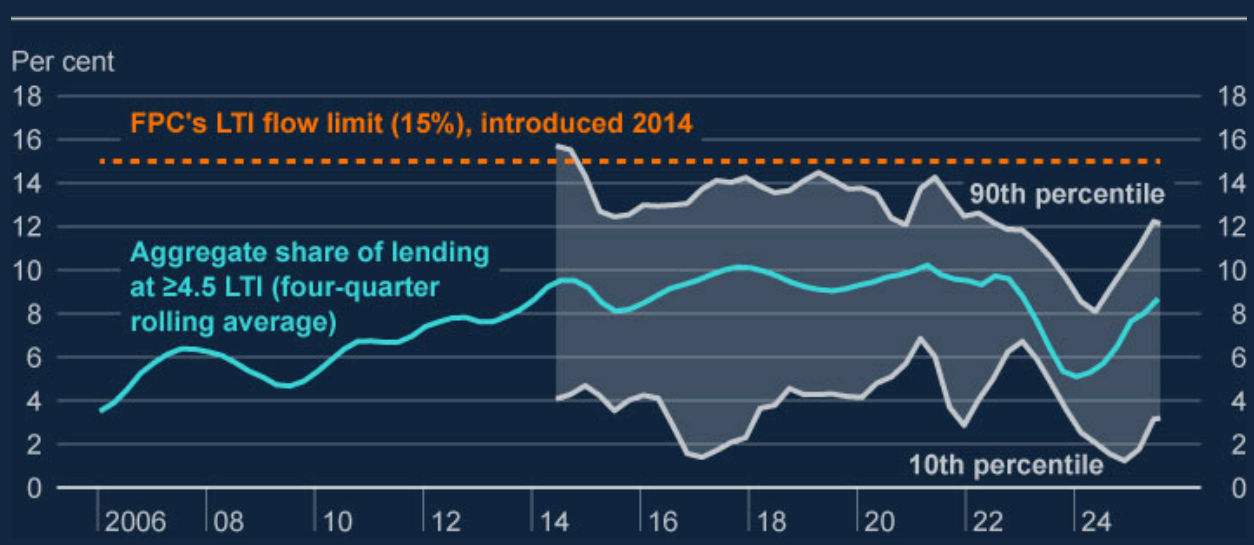
reduce risks to financial stability that could arise from the mortgage market. The FPC measure and FCA rules have helped keep aggregate DSRs and arrears below the levels seen during the GFC, even in the recent period of rising interest rates.

The FCA published a **clarification** in March 2025 around the stress rate component of its MCOB rules. In addition, the FPC updated its **Recommendation** to the Prudential Regulation Authority (PRA) and FCA in Q2 to ensure the LTI flow limit is implemented proportionately. This amendment allows individual lenders to increase their share of lending at high LTI ratios while aiming to ensure the aggregate flow remains consistent with the limit of 15%. Consistent with the FPC's update, the PRA has provided an interim **modification by consent** that allows approved lenders to disapply the 15% LTI flow limit in PRA rules with immediate effect. This adjustment in requirements allows individual lenders more flexibility to go above the 15% limit in line with their own risk frameworks and subject to the aggregate level across all lenders remaining consistent with the 15% limit.

It remains too early to assess the full impact of these policy changes on the mortgage market. However, several major lenders have already changed their behaviour in response to the MCOB statement, in part driving a fall in median stress rates on Q3 completions of around 100 basis points since Q1. Consistent with this, indicators from the **Credit Conditions Survey – 2025 Q3** and market intelligence point to a higher supply of credit to households. And net mortgage approvals hit a nine-month high in September, returning to the pre-Covid average (Section 4). The share of high LTI lending increased to 9.5% in Q3, in line with Q1 and up from 7.6% in Q2, which was depressed by the end of the stamp duty land tax holiday. This leaves the four-quarter rolling average at 8.7%, well below the 15% limit (Chart 3.2). The FPC will continue to monitor the effect of the policy changes on the housing market.

Chart 3.2: High LTI lending increased in 2025 Q3

The share of new lending at ≥4.5 LTI (a) (b) (c)



Sources: FCA Product Sales Data and Bank calculations.

(a) The FPC's flow limit applies on a four-quarter rolling average basis.
(b) Range of lenders' share of lending at greater than or equal to 4.5 LTI (four-quarter rolling average) constructed using the weighted 10th to 90th percentiles of firms' use of their individual flow limits and shown from the introduction of the FPC's flow limit in 2014 Q4.
(c) The sample includes only all new mortgages for house purchases and external remortgages with a change in principal.

While looser credit conditions allow additional borrowers to enter the market in the near term, **staff analysis** suggests that, unless there is also an increase in housing supply, increased credit availability has limited ability directly to address barriers to home ownership. The FPC supports initiatives to explore increases in the supply of housing and greater access of creditworthy households to mortgages, including at higher loan to values (LTVs).

> **The FPC judges that, in aggregate, households remain resilient. It would take significant falls in household incomes and rises in interest rates for the aggregate debt-servicing burden to rise materially.**

Staff scenario analysis suggests that it would take a substantial shock to both incomes and lending spreads for the aggregate mortgage DSR to reach its GFC peak. Therefore, the FPC expects UK households to remain resilient in aggregate. The results of the 2025 Bank Capital Stress Test suggest that UK banks would have capacity to continue supporting household lending even if economic conditions turn out materially worse than expected (Section 5).

3.3: UK corporate debt vulnerabilities

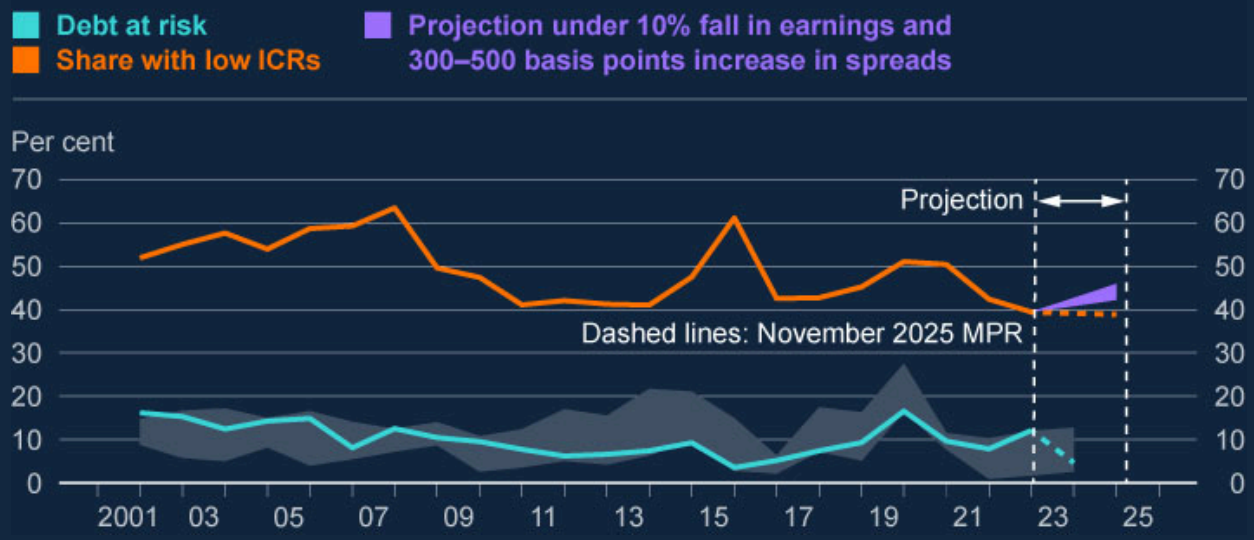
Measures of indebtedness suggest UK corporates remain resilient in aggregate. And the share of vulnerable corporates has remained steady compared to Q2, well below historical peaks.

The corporate net debt to earnings ratio ticked up slightly in 2025 Q2 as net debt increased and profits fell slightly. At 134%, the aggregate ratio remains well below Covid (166%) and post-GFC (230%) highs, reducing the risk that indebted corporates would materially amplify a shock relative to the past. However, this aggregate picture can mask vulnerabilities within particular companies and sectors. Despite global uncertainty (including from the US credit market), historically tight credit spreads mean that current funding conditions are benign. But a sharp correction could constrain refinancing options for UK corporates.

The share of highly indebted corporates that would struggle in the event of an income or interest rate shock has remained largely stable compared to the July FSR. Both the debt-weighted proportion of corporates with low interest coverage ratios (ICRs), and the Bank's broader **corporate debt at risk** measure remain well below historical peaks (Chart 3.3). Sensitivity analysis by Bank staff shows that it would take a very severe shock to funding costs and corporate earnings to reach historic peaks.

Chart 3.3: Measures of corporate vulnerability would remain low even if earnings fell substantially and funding costs increased

Debt-weighted share of UK corporates with ICRs below 2.5 and share of UK corporates at higher risk of default and staff projections (a) (b) (c) (d) (e)



Sources: Moody's: Bureau van Dijk and Bank calculations.

(a) These data refer to UK private non-financial corporations only.
(b) The central case ICR projection conservatively assumes full pass-through of the Bank Rate path to the stock of floating and maturing fixed rate corporate debt over 2025. The projection uses the OIS curve Bank Rate as of 24 November 2025. The stressed projection assumes a 10% fall in earnings and a range of 300 to 500 basis points increase in corporate lending spreads.
(c) The aqua line represents the debt-weighted share of UK corporates that simultaneously breach the three thresholds associated with the highest likelihood of firm failure: whether a company's ICR, calculated by dividing its earnings before interest and tax, is below 2.5; whether its liquidity ratio (current ratio) is below 1.1; and whether its return on assets is negative. Partial data in 2024.
(d) Alternative projections of debt at risk within the swathe capture firms that breach any three thresholds within six factors (the three set out in (c), as well as turnover growth less than -5%, leverage growth greater than 5% and leverage less than 1) and breach the thresholds with the highest marginal effects. **Stressed or in distress? How best to measure corporate vulnerability**.
(e) The historical time series of debt at risk and of companies with low ICRs are different to those published in the July FSR due to changes in data and methodology.

Consistent with the low share of vulnerable corporates, monthly insolvency rates were at a low level at around 53 per 10,000 firms in the 12 months to September 2025, well below their long-term average level of around 70 per 10,000 firms, and lower than the rate recorded in September 2024.

However, there has been an uptick in insolvencies for medium-sized corporates, although most insolvencies are still driven by small firms with limited debt and employment. There have not been any high-profile company defaults in the UK as seen in the US, and spillovers to the UK from the defaults of Tricolor and First Brands Group have been limited (Section 2). The current rate of UK insolvencies is unlikely to pose borrower or lender resilience challenges.

Small and medium-sized enterprises (SMEs) remain under more pressure than larger corporates and arrears for non-government guaranteed debt have been rising slowly for the past two years.

SME arrears for non-government guaranteed debt have been gradually rising over the past couple of years and increased in August by 0.2 percentage points to 1.5%. The share of SMEs in arrears is highest in the accommodation and food, construction, and retail trade sectors, which are more exposed to increased input costs and increased labour market costs associated with a higher minimum wage and the increase in employer's national insurance contributions (NICs). Around 10% of SMEs are currently using their overdraft facilities, similar to pre-Covid averages. However, SME lending has limited implications for banking system losses in aggregate because their bank exposures are relatively small, and a portion of this lending is government guaranteed. Refer to Box B for more information on lending to the real economy over the longer-term, including to SMEs.

Some highly leveraged corporate borrowers relying on market-based finance areparticularly exposed to tighter financing conditions, which could be triggered by global shocks.

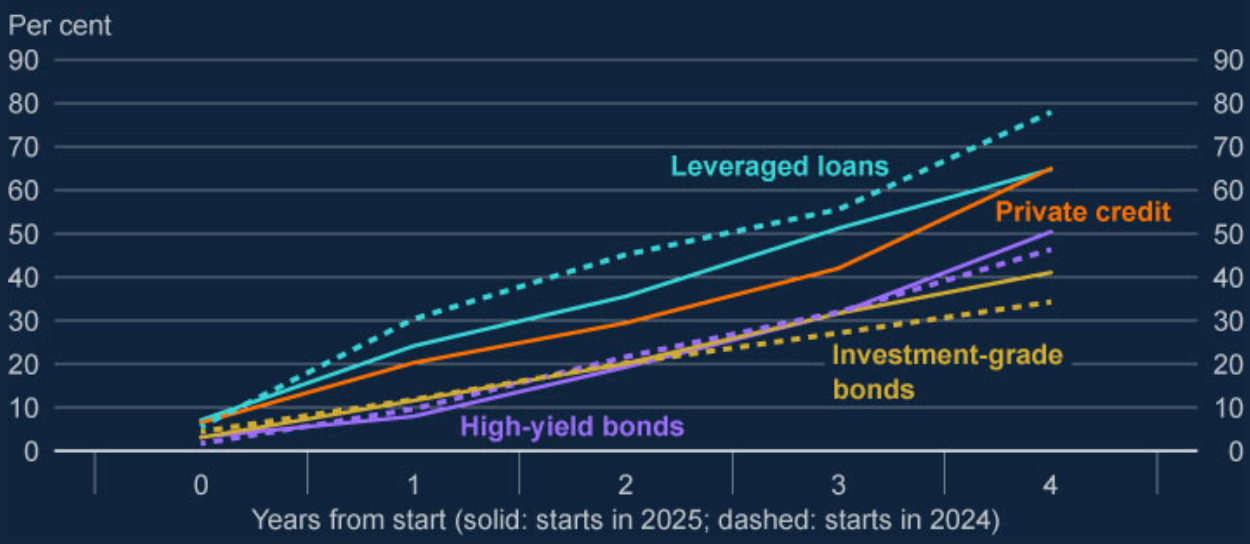
UK corporates borrowing via market-based finance, such as leveraged loans, high-yield bonds and private credit, might face refinancing challenges due to higher interest rates and greater borrowing levels. Lower realised and expected interest rates will have eased some refinancing pressures. And despite global uncertainty, historically tight credit spreads indicate that current corporate funding conditions are benign. However, the likelihood of tightening in market conditions has increased. A sharp correction in credit spreads could significantly constrain financing options for UK corporates, particularly those facing imminent refinancing needs.

While interest rates remain high, cuts in Bank Rate will have benefitted corporates on floating interest rates (eg variable-rate bank loans) that decreased in line with Bank Rate. However, higher interest rates may have not yet passed through to a subset of corporates, largely those relying on market-based finance (or with interest rate hedges in place), which make up a significant proportion of UK corporate debt (Box B).

Corporate bonds, which comprise a large part of total market-based financing in the UK, are fixed for 10 years on average, meaning issuers are likely to face interest rate increases as they refinance. However, most publicly issued bonds are investment grade, and their issuers are likely to be more resilient to higher rates because of low leverage, stronger balance sheets and more choice over sources of finance. Near-term refinancing requirements in Q3 were contained for UK bond issuers, broadly in line with the maturity walls from 2024 Q3 (Chart 3.4).

Chart 3.4: Refinancing walls are steeper for riskier credit markets, like leveraged loans and private credit

Cumulative share of debt maturing by type, per cent (a) (b)



Sources: Pitchbook LCD, Refinitiv Eikon from LSEG and Bank calculations.

(a) The chart captures market-based finance debt issued in all currencies by UK corporates, both UK issuer with a UK parent and UK issuer with a non-UK parent. Annual estimates.
(b) Dashed lines represent data from the 2024 Q3 vintage; solid lines represent data from the 2025 Q3 vintage.

Refinancing walls are steeper in markets serving higher-risk borrowers, such as leveraged loans and private credit, where terms tend to be shorter. In Q3, around a quarter of outstanding leveraged loan debt was due to mature by the end of next year, and over half was due to mature by end-2028, slightly less than the shares in 2024 Q3. Private credit shows similar dynamics, with around 20% due by next year and 42% by end-2028. The steeper refinancing walls increase the exposure of these corporates to higher interest rates and deteriorations in investor risk sentiment. These markets are also more vulnerable to higher spreads as, historically, spreads tend to increase more in risky markets in a stress.

Credit spreads across a range of markets widened marginally in November compared to the previous month, partly as a response to the recent high-profile US corporate defaults, but they remain very low by historical standards (Section 2). This has reduced corporate borrowing costs, encouraging higher levels of corporate issuance and easing refinancing burdens. However, given elevated global uncertainty, the risk of a sharp correction remains high. Deterioration in market sentiment could increase spreads and reduce the availability of funding, heightening refinancing challenges, especially for highly leveraged or lower-rated corporates.

Private equity-backed corporates are particularly vulnerable, as a large proportion of these corporates have high levels of debt and are financed by riskier credit markets like private credit and leveraged loans. The Bank's second system-wide exploratory scenario (SWES) will explore risks and dynamics associated with the private market ecosystem (Section 6).

Businesses facing higher debt-servicing costs after refinancing, or difficulties in sourcing finance, may take defensive action by cutting back on investment and employment and may be more likely to default. Because firms using riskier forms of market-based finance comprise at least 12% of UK employment, stress in these markets could pose some borrower and lender resilience challenges.

The FPC judges that, in aggregate, the UK corporate sector is resilient.

Overall, the FPC expects that corporates will remain resilient in aggregate. But the potential interconnected shocks in global financial markets that they could be facing could increase the likelihood of core vulnerabilities crystallising. There are still pockets of vulnerability among SMEs and highly leveraged corporates, including private equity-backed businesses.

The results of the 2025 Bank Capital Stress Test suggest that the UK banking system could continue to support lending and growth for creditworthy corporates even if economic conditions turn out materially worse than expected (Section 5).

4: UK banking sector resilience

4.1: Recent developments in UK banks' resilience

The UK banking system remains well capitalised to support lending and growth, and the FPC has updated its assessment of the appropriate level of bank capital.

The UK banking system remains well capitalised, and UK banks' aggregate Common Equity Tier 1 (CET1) capital ratio is little changed since the July FSR (Table 4.A). Considered over a longer time horizon, the aggregate CET1 capital ratio has been broadly stable since the completion of the phase-in of the post-global financial crisis (GFC) bank capital framework in 2019. Following its first assessment in 2015, and a subsequent update in 2019, the FPC has updated its assessment of the appropriate level of bank capital requirements, which is covered in detail in Box D and the **Financial Stability in Focus**.

Table 4.A: Selected indicators of banking sector resilience (a) (b)

	Latest	July 2025 FSR
CET1 capital ratios		
Major UK banks (c)	14.4% (Q3)	14.4% (Q1)
Small and medium-sized UK banks	18.1% (Q3)	18.3% (Q1)
Liquidity coverage ratios		
Major UK banks (three-month moving average)	147% (October)	152% (May) (d)
Small and medium-sized UK banks (three-month moving average)	277% (September)	285% (May)
Asset quality		
Loans for which there has been a significant increase in credit risk since origination (IFRS 9 'Stage 2') (major UK banks)	9.4% (Q3)	9.6% (Q1) (d)
Provisions as a share of lending (major UK banks)	0.89% (Q3)	0.92% (Q1) (d)

Sources: PRA regulatory returns, published accounts and Bank calculations.

(a) The major UK bank peer group includes the following banks: Barclays, HSBC, Lloyds Banking Group, Nationwide, NatWest Group, Santander UK and Standard Chartered Bank.
(b) The small and medium-sized UK banks series represents the aggregate of a group of PRA supervised non-systemic UK banks and building societies.
(c) The aggregate Tier 1 capital ratio for major UK banks was 17.2% in both 2025 Q1 and Q3.
(d) Figures reflect revisions subsequently made by banks after the data cut-off date for the July FSR.

Major UK banks continued to report robust earnings, their asset quality remains strong, and they have been returning capital to shareholders.

Major UK banks reported underlying return on tangible equity (RoTE) of 14.7% in Q3 2025, and consensus expectations are for aggregate RoTE to rise a little above its current level over the coming years.[7] Several banks upgraded their earnings guidance for 2025 in Q3, and there was a broad-based upgrade to consensus estimates following Q3 earnings. Major UK banks continued to return capital to shareholders through buybacks and dividends, totalling £8.6 billion in Q3.

Major UK banks' asset quality remained strong in Q3, with little change in aggregate relative to the July FSR (Table 4.A), despite some banks increasing impairments on specific portfolios. Nevertheless, two recent high-profile corporate defaults in the US highlighted a number of potential weaknesses in risky credit markets previously flagged by the FPC. These include high leverage, weak underwriting standards, opacity, complex structures, and the degree of reliance on credit

rating agencies, and illustrate how corporate defaults could impact bank resilience and credit markets simultaneously. UK banks' direct and indirect exposures to First Brands and Tricolor are limited. The Bank's second system-side exploratory scenario (SWES) exercise will explore risks and dynamics associated with the private markets ecosystem, including interlinkages between banks and non-bank financial institutions (NBFIs) active in those markets, under a stress scenario (Section 6).

Some lenders continue to face the potential for redress payments in respect of past motor finance commission arrangements. In October, the FCA published its **consultation** on the redress scheme for motor finance consumers. The FCA estimates total sector-wide costs of £11 billion, of which all banks, including the major UK banks, account for 51% of total costs (with lenders owned by vehicle manufacturers accounting for most of the remainder). The FCA's consultation closes on 12 December. If it decides to introduce a redress scheme, it expects to publish its policy statement and final rules in early 2026.

> **UK bank valuations are near post-GFC highs, supported by a decline in their cost of equity and an increase in expected RoTE.**

UK banks' average price to tangible book (PtTB) ratios have increased further above one since the July FSR, up from Covid-era lows of around 0.5.[8] As set out in the **June 2024 FSR**, PtTB ratios are an indicator of expected future shareholder returns relative to their cost of equity (the compensation investors require for the perceived riskiness of those returns). Valuations of major UK banks have increased due to both an increase in expected aggregate RoTE and a decrease in their cost of equity in recent years.

Chart 4.1: Major UK banks' aggregate PtTB ratio has continued to rise since the July FSR, and is at a similar level to that of euro-area banks but lower than US banks

PtTB ratios for UK, euro area, and US bank indices (a) (b) (c)

Sources: Bloomberg Finance L.P. and Bank calculations.

(a) The UK series is a weighted average (by tangible book value) for Barclays, HSBC, Lloyds Banking Group, NatWest Group and Standard Chartered Bank.
(b) The euro-area series is a weighted average (by tangible book value) for the Eurostoxx Banks (SX7E).
(c) The US series is a weighted average (by tangible book value) for constituents of the S&P 500 banks index plus Goldman Sachs and Morgan Stanley.

While UK bank PtTB valuations remain below those of US banks (Chart 4.1), the difference between the one-year forward price-to-earnings ratios of major UK banks and US banks is broadly in line with that for other sectors.[9] This suggests that market-wide factors continue to be a significant driver of UK banks' valuations relative to those of US banks, as set out in the **June 2024 FSR**.

UK banks have high levels of liquidity and have continued to adjust to the normalisation of the Bank's balance sheet.

Aggregate three-month moving average Liquidity Coverage Ratios (LCRs) have reduced slightly since the July FSR (Table 4.A). However, the UK banking system has maintained high levels of liquidity. The normalisation of the Bank's balance sheet has continued as the extraordinary measures put in place following the GFC and Covid pandemic have been unwound further. The Bank's Asset Purchase Facility holdings and the Term Funding Scheme with additional incentives for SMEs (TFSME) are winding down. In October, banks repaid £30 billion of TFSME drawings as they fell due. This brings the outstanding TFSME amount to £42 billion from £193 billion outstanding in 2021. As expected, gilt repo rates rose temporarily at the end of October, in part due

to the reduction in reserves, but retraced following usage of the Bank's facilities. Use of the Bank's facilities, including the Indexed Long-Term Repo (ILTR) and Short-Term Repo (STR), has continued to increase as intended.

4.2: UK banks' provision of credit to households and businesses

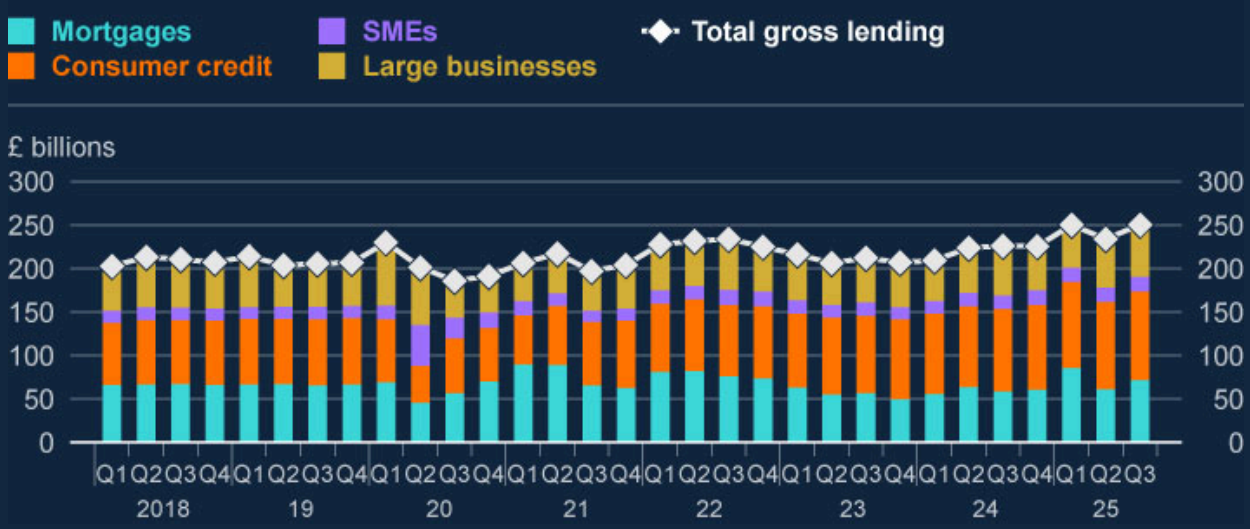
> **Aggregate lending has continued to increase year-on-year, with gross household and corporate lending flows above or around pre-Covid levels.**

The mortgage market remains competitive: lending spreads over risk-free rates are around pre-GFC levels and the range of products at higher loan to value (LTVs) and loan to income (LTI) ratios continues to exceed pre-Covid levels. Following a decline in 2025 Q2 that reflected the impact of buyers bringing mortgage purchases forward to Q1 ahead of the stamp duty changes, mortgage activity picked up in Q3, including the proportion of new loans at higher LTI and LTV ratios. This was driven by stronger-than-expected demand and an easing in lending conditions. Some of this easing reflected banks reducing stress rates on mortgage lending in response to the FCA's clarification of its Mortgage Conduct of Business (MCOB) rules (Section 3). Looking forward, there may be further increases in lending at higher LTV and LTI ratios as the full impact of the FCA clarification feeds through, along with effect of the adjustment made by the PRA to the application of the LTI flow limit, following the FPC's updated recommendation in Q2 (Section 3). This is supported by evidence from the most recent **Credit Conditions Survey – 2025 Q3** (CCS), where lenders reported expectations of further increases in mortgage availability in Q4.

Lending by banks to large corporates and SMEs has continued to increase since the July FSR, with SMEs recording four consecutive months of annualised net lending growth for the first time since 2021. There have been improvements in the availability of credit for corporates, with lenders reporting increases in the CCS, and the Bank's Agents corroborating this. Agents now assess supply conditions to be normal for small businesses and above normal for medium and large corporates, with competition amongst bank and non-bank lenders for lending to creditworthy businesses. Increased competition is said to be contributing to compressed spreads and an easing in some loan terms. Demand for borrowing by corporates is judged by the Agents to be below normal, reflecting subdued investment given the economic outlook and high interest rates. But the Agents note some pockets of increased demand, and lenders noted a slight increase in demand in the CCS. Although lending data for Q4 is not yet available, lenders reported expectations of increases in the demand for and availability of corporate credit in the CCS. There are also structural factors that continue to influence levels of credit provision to SMEs (Box A).

Chart 4.2: A fall in gross lending volumes from banks and building societies in 2025 Q2 reflected the impact of mortgage activity brought forward to the first quarter. Lending volumes then recovered in the third quarter

UK monetary financial institutions' gross lending to UK households and businesses, seasonally adjusted (a) (b) (c)



Sources: Bank of England and Bank calculations.

(a) Lending to UK households and businesses by banks and building societies who have permission to accept deposits in the UK.
(b) SMEs are defined as businesses with annual debit account turnover on the main business account up to £25 million. Large businesses are those with annual debit account turnover on the main business account of over £25 million.
(c) Seasonally adjusted data.

The easing of credit conditions has been in line with the macroeconomic outlook, with some additional easing in the mortgage market related to policy developments.

In its assessment of what has driven changes in credit conditions, the FPC considers a range of factors. These include the quantity, quality and price of credit available; indicators of the macroeconomic environment; and indicators of demand including from the credit conditions survey. The FPC also considers the resilience of the UK banking system, which remains well capitalised. Taking these factors into consideration, the FPC judges that overall developments in credit conditions continue to reflect the macroeconomic outlook.

The FPC has maintained the UK countercyclical capital buffer (CcyB) rate at its neutral setting of 2%.

In making this decision the FPC takes into account a number of principles, as set out in the **FPC's approach to setting the countercyclical capital buffer – Policy Statement**. Although the global risk environment remains elevated, UK household and corporate aggregate indebtedness remains

low. The easing of credit conditions since the FPC's Q3 meeting has been in line with the macroeconomic outlook, with some additional easing in the mortgage market related to policy developments.

The FPC has decided this quarter to maintain the UK CCyB rate at its neutral setting of 2%. Maintaining a neutral setting of the UK CCyB in the region of 2% should help to ensure that banks continued to have capacity to absorb unexpected future shocks without an unwarranted restriction in essential services, such as the supply of credit, to the UK real economy.

The FPC will continue to monitor the evolution of financial conditions closely to ensure the setting of the CCyB remains appropriate.

4.3: Interlinkages with non-bank financial institutions

> **Interlinkages between banks and NBFIs play a critical role in supporting the functioning of the financial system. However, these connections also introduce risks, particularly as their size and complexity have grown significantly in recent years.**

When effectively managed, relationships between banks and NBFIs support market-based finance and other forms of credit provision to businesses. In addition, these interlinkages play a critical role in maintaining market functioning – banks' liquidity provision to NBFIs, especially during periods of stress, is important to support market functioning in core UK markets.

Previous FSRs in November 2024 and July 2025 have covered the potential risks to banks from their relationships with different types of NBFIs. This has included risks from private equity counterparties as well as hedge funds and other leveraged counterparties. These risks include counterparty credit risks, credit risks, liquidity and funding risks and market risks, which could result in losses for banks with direct exposures (Figure 4.1).

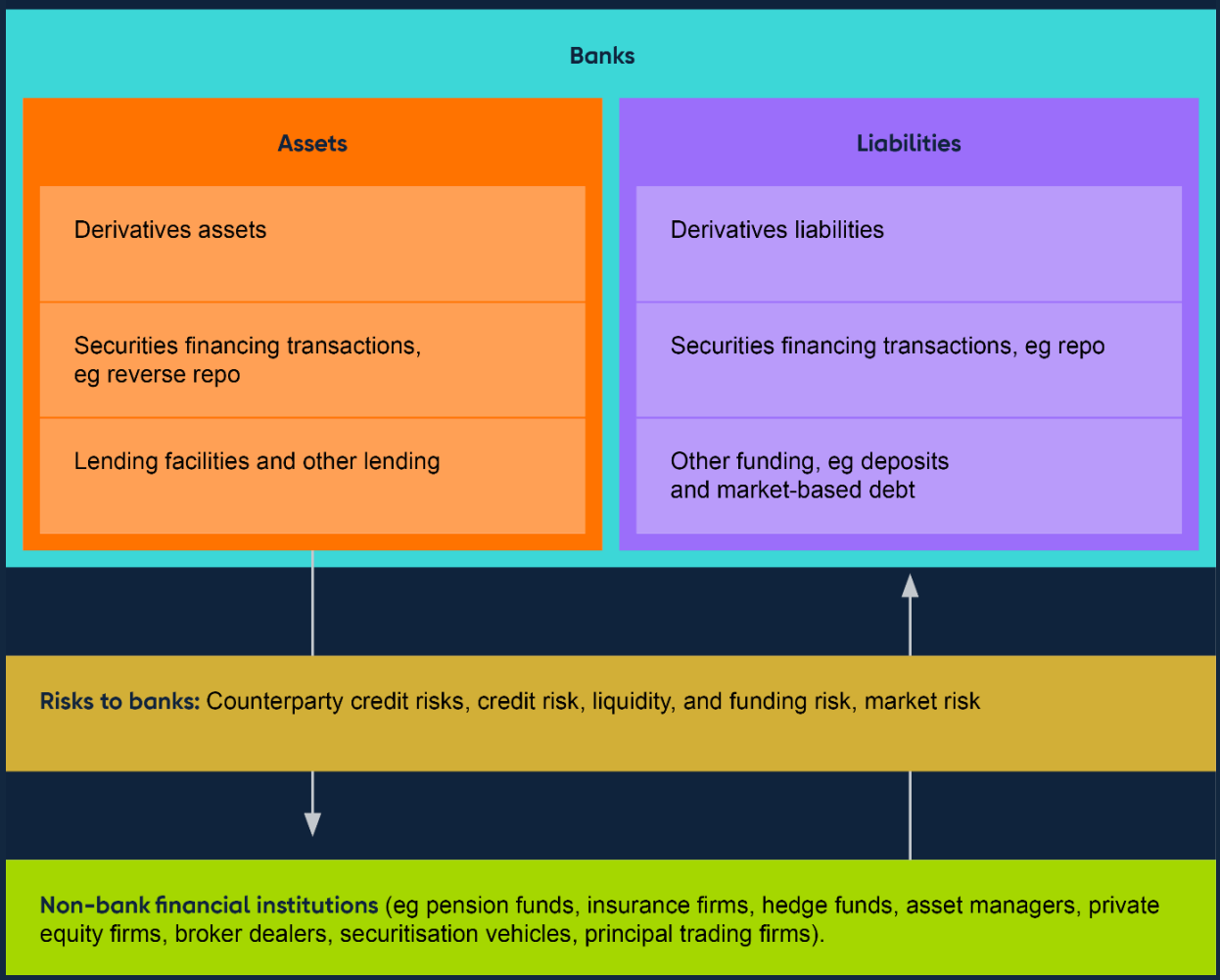
> **Principal trading firms are another category of NBFIs that banks provide services to. Their high-speed, high-volume intraday transactions create specific risks for these banks.**

Principal Trading Firms (PTFs) are a type of NBFI that typically uses low latency trading strategies. These market participants are important market-makers and growing providers of short-term liquidity in UK and global markets.

Banks provide PTFs with market access, execution, clearing, settlement and financing services. As PTF activities often involve high volumes of intraday trading, this can result in banks' intraday exposures, through their PTF clients, exceeding end-of day positions. Given the sophistication needed to measure and manage these exposures, PTF counterparty exposures are primarily concentrated amongst banks who specialise in this area. Should there be simultaneous defaults across multiple major PTFs, this could lead to losses for these banks, though collateral mitigates some of this risk. As PTFs have grown in scale and market footprint, there has been broadening in their financial resources and financing providers. As new banks enter this space and others expand the services they provide to PTFs, they must appropriately manage these unique counterparty risk exposures.

It is important that UK banks ensure appropriate risk management of their exposures to NBFIs, including PTFs. The PRA's 2025 list of priorities for UK Deposit Takers raised counterparty credit risk as a continued area of focus, in particular exposures to NBFIs.[10] The Basel Committee on Banking Supervision has previously set out guidelines to strengthen banks' management of counterparty credit risks, including from NBFIs.[11]

Figure 4.1: There are multiple channels through which direct NBFI exposures could pose risks to banks' balance sheets



Box D: The FPC's assessment of bank capital requirements

This box sets out the key analysis and judgements taken by the FPC as part of the **Committee's assessment of the appropriate level of capital requirements for UK banks**, which is published alongside this Financial Stability Report. This assessment complements other work the FPC is undertaking to support sustainable UK growth, and is part of ensuring that measures supporting the FPC's primary objective to promote UK financial stability are operating effectively and efficiently as the financial system evolves (Section 1 and Box A).

> **The UK banking system plays a vital role in the economy by providing lending and financial services to households and businesses right across the country. It is crucial that it is resilient enough to support UK growth, in good and bad times.**

Ensuring a resilient financial system – one which can absorb rather than amplify shocks – is the most important contribution the FPC can make, not only to promote financial stability, but also to support economic growth. Periods of financial instability negatively impact the provision of vital services, weighing on output growth, as observed during and after the global financial crisis (GFC). Conversely, financial stability underpins the continued provision of vital financial services and contributes to a stable and predictable economic environment. This in turn supports consumer and business confidence, facilitates investment that drives long-term productivity growth, makes the UK an attractive place to do business for international investors and supports UK firms' ability to compete abroad.

The banking system is a critical part of the financial system. Banks' liabilities largely take the form of money deposits, which underpin vital banking and payment services. Most money in the financial system is held as commercial bank deposits. The assurance of its fixed nominal value is key to maintaining financial stability and public trust. During the GFC, it was uncertainty about the future solvency of banks that undermined this trust and thus financial stability.

Banks also account for around 85% of lending to UK households and just under half of lending to UK corporates. And they play an increasingly significant role in supporting market-based finance, including through the provision of lending and other services to various types of non-bank financial institutions.

Given the significance of these activities, a key objective of the FPC is to ensure that the banking system is appropriately capitalised to support sustainable growth over the long term. This will ensure that it can support households and businesses in good and bad times.

The FPC first assessed the appropriate level of capital requirements for the banking system in 2015, drawing on published analysis of the macroeconomic costs and benefits of capital by Bank staff. The FPC judged that the appropriate benchmark level for system-wide Tier 1

capital requirements was around 14% of risk-weighted assets (RWAs), once gaps and shortcomings in the measurement of RWAs and the neutral rate for the UK component of the countercyclical capital buffer (henceforth UK CCyB) were accounted for.[12] This was lower than other estimates of the optimal level of capital, and in many cases, materially so. In large part, that reflected key judgements relating to the effectiveness of post-crisis reforms, including on the credibility and effectiveness of the bank resolution regime, effective supervision and structural reform, and the Committee's intention to use the CCyB actively, without which the FPC's assessment of the appropriate level of capital would have been materially higher. In 2019, the FPC reaffirmed its 14% benchmark.

> **The FPC has revisited its assessment of the appropriate capital requirements for the banking system from the perspective of the costs and benefits to growth.**

This assessment weighs the macroeconomic costs of capital, which stem from the impact of higher capital pushing up on borrowing costs, against the benefits of capital, which come about because higher bank capital reduces the likelihood and costs of financial crises. The Committee has taken into account the experience of the 10 years since it first assessed the appropriate overall level of capital.

> **The Committee judges that the appropriate benchmark for the system-wide level of Tier 1 capital requirements is now 1 percentage point lower at around 13% of RWAs – equivalent to a Common Equity Tier 1 (CET1) ratio of around 11%.**

This 13% benchmark for Tier 1 capital requirements comprises an underlying optimal level of 11%, inclusive of the neutral rate for the UK CCyB, and an additional 2 percentage points to account for outstanding gaps and shortcomings in the measurement of RWAs. Pillar 2A minimum requirements, which capture such gaps and shortcomings, mean that UK banks have capital for risks such as interest rate risk in the banking book, the importance of which was highlighted by the failure of Silicon Valley Bank in 2023.

Given the reduction in the FPC's benchmark, banks should have greater certainty and confidence in using their capital resources to lend to UK households and businesses.

> **That judgement is consistent with the evolution in the financial system since the FPC's first assessment, including a fall in banks' average risk weights, a reduction in the systemic importance of some banks, and improvements in risk measurement.**

In undertaking its review, the FPC considered how capital requirements have evolved since previous assessments and feedback it has received from the industry and other stakeholders. It noted that:

- average risk weights have fallen as banks have changed the composition and riskiness of their balance sheets. The 7½ percentage point fall in banks' average risk weights (measured excluding central bank reserves) since the beginning of 2016 means that the FPC's previous Tier 1 benchmark is now associated with around £60 billion less nominal

capital, based on the size of current balance sheets, than would have been the case absent the fall in risk weights;

- systemic buffers are lower than envisaged in 2015 as some banks have decreased in systemic importance; and
- the implementation of Basel 3.1 on 1 January 2027 will improve risk measurement, allowing the Prudential Regulation Authority (PRA) to reduce Pillar 2A minimum requirements by around ½ percentage point. As a result, the level of system-wide Tier 1 capital requirements is expected to fall to around 13% of RWAs when Basel 3.1 is implemented, consistent with the FPC's updated benchmark.

The FPC considers that the inbuilt responsiveness of nominal capital requirements in the banking system – to falls in average risk weights, decreases in UK banks' systemic importance, and improvements in the measurement of risk weights – reflects desirable flexibility in the capital framework.

Flexibility in the framework means that capital requirements can continue to respond to developments in underlying structural and cyclical factors in future, including if risk levels were to change.

UK banks have tended to have capital headroom over regulatory minimum and buffer requirements.

Currently, banks in aggregate have CET1 capital resources of about 2% of RWAs over their requirements, although such 'capital headroom' varies considerably across banks and over time. While the PRA and FPC have no requirements – formal or informal – for capital headroom, banks maintain this additional capital for a number of reasons, including a perceived lack of buffer usability.

The level of risk-based capital requirements for large banks in the UK is broadly similar to that in the euro area. And analysis that attempts to adjust for some key differences in the way risks are captured between the UK and US suggests that the level in the UK is lower than that in the US. That said, UK requirements appear to be higher than in other jurisdictions for some more specific aspects and cohorts, particularly leverage ratio requirements for large domestically focused banks.

Comparing capital requirements across jurisdictions is challenging given differences in how risks are captured in different regulatory frameworks and the FPC would welcome feedback on its approach. In particular, the US framework differs in important respects from the UK – for example, the UK and EU regulatory frameworks capture some risks through Pillar 2 capital add-ons, while the US framework under law instead tends to apply higher risk weights. There are also differences in the characteristics of individual banks, such as how systemically important they are, that help account for differences across jurisdictions.

The Committee considers that its updated benchmark is consistent with its view that the banking sector can support long-term growth in the real economy in both current and adverse economic environments.

Since the FPC's previous assessments, the banking system has supported the real economy through several macroeconomic shocks, including those related to Covid and Russia's invasion of Ukraine. This stands in contrast to the behaviour observed during the GFC when bank deleveraging was a material source of amplification. During the Covid pandemic, well-capitalised banks were able to extend credit to businesses, as well as granting payment holidays to mortgagors. As the economic outlook improved following recent shocks, credit conditions for households and businesses improved commensurately and have since evolved in line with the macroeconomic outlook. Mortgage lending spreads over risk-free rates are around pre-GFC levels, and the Bank's Agents assess credit supply conditions to be normal for small businesses and looser than normal for medium and large corporates, with competition among bank and non-bank lenders to lend to creditworthy businesses (Section 4).

The results of the 2025 Bank Capital Stress Test (Section 5) suggest that the banking system is sufficiently well capitalised to continue lending to creditworthy households and businesses in a severe but plausible macroeconomic stress, with significant headroom over hurdle rates in aggregate at the low point of the test. Most of this headroom is accounted for by the fact that banks start the test with capital in excess of regulatory requirements and buffers.

Higher returns on tangible equity (RoTE) – and investors' increasing confidence that those returns can be sustained – have supported a material increase in UK banks' equity market valuations (Section 4). Major UK banks' average price to tangible book ratio is above 1, indicating that investors expect RoTE to be above the level needed to compensate them for the perceived riskiness of those returns (referred to as the 'cost of equity'). Relatedly, there is evidence that the premium investors demand to hold UK banks' equity relative to their debt has fallen, which reduces the cost to banks of increasing their share of equity funding relative to debt funding, all else equal. Major UK banks have also continued to return capital to shareholders through buybacks and dividends, totalling around £90 billion over the past three years.

> **The Committee's updated benchmark remains in the range of capital requirements likely to maximise macroeconomic net benefits in terms of long-run growth, albeit towards the lower end. Analysis suggests that materially lower capital requirements could lead to significant reductions in long-run expected GDP.**

The FPC has considered updated evidence related to its previous judgements on the economic costs and benefits of capital and reviewed external academic studies that provide independent estimates of optimal capital levels.

The FPC reaffirms that its previous judgements related to the positive impact of post-crisis reforms remain appropriate. Those judgements were related to credible and effective resolution arrangements, effective supervision, structural reform such as the implementation

of ring-fencing, and the Committee's active use of the time-varying CCyB. Together, these judgements materially reduced the FPC's assessment of the appropriate level of capital in 2015.

Updated analysis suggests that the macroeconomic costs of bank capital may have declined as the spread between banks' cost of equity and the cost of their debt has fallen. At the same time, various developments may have impacted the macroeconomic benefits of bank capital. Global vulnerabilities, including risks associated with sovereign indebtedness, have increased. But conversely, the indebtedness of UK households and businesses has fallen, and banks' underwriting standards have improved.

Analysis of the net macroeconomic impact of capital requirements suggests that the Committee's updated benchmark is within, albeit towards the lower end of, the range of capital requirements that are likely to maximise expected long-term growth. The FPC's updated benchmark is also at the lower end of the range of optimal capital levels estimated in the external academic literature.

Analysis also suggests that reducing system-wide capital requirements materially below the FPC's updated benchmark of 13% (unless due to further improvements in risk measurement that allow overlaps to be removed from Pillar 2A requirements) could be associated with significant reductions in long-run expected GDP through the costs of greater instability – especially if those reductions in capital were to undermine the credibility of the resolution regime as a result of lower overall loss-absorbing capacity. Materially lower capital levels could also lead to higher risk premia on bank funding costs, which would in turn feed through to higher borrowing costs and lower investment by businesses.

> **The FPC has also considered whether the capital framework might warrant adjustment to make it more effective, efficient and proportionate in the future, and to address any unintended consequences.**

The capital framework has a number of constituent parts, intended to address different risks banks face or pose. Minimum capital requirements aim to ensure banks operate with an adequate layer of capital to enable an orderly failure, maintain market confidence and protect depositors without losses to taxpayers. Buffers help ensure that even in times of stress, banks have sufficient capacity to absorb losses, and so can continue to support the real economy. Requirements apply on a risk-weighted as well as a simpler leverage basis – the leverage ratio guarding against excessive leverage and potential inaccuracy in the way banks measure risk.

Developments over the past decade, lessons on how the bank capital framework operates in stress, and feedback provided by industry and other stakeholders, suggest there are ways in which some parts of the capital framework could be adjusted to support growth while maintaining appropriate resilience.

To that end, significant steps are already being taken to address feedback and improve the efficiency and proportionality of the framework. These include: the Bank reducing the frequency of its main stress tests of capital resilience from annual to biennial; the finalisation of Basel 3.1 reforms; steps taken by the PRA to enhance the proportionality of the framework for smaller lenders, including through the recently published Strong and Simple framework; and the uprating of some regulatory thresholds.[13]

The FPC has approached the present assessment of capital requirements proactively and has identified further broad, material categories of issues in which it supports further work to assess whether changes could make the capital framework more effective, efficient and proportionate. The FPC would expect banks to use any such changes as a means to increase their support of households and businesses in the real economy.

> **With the PRA and international authorities, the FPC will work to enhance further the usability of regulatory buffers, and so reduce banks' incentives to have capital in excess of regulatory requirements and buffers.**

Regulatory capital buffers make up just under half of risk-weighted capital requirements and are explicitly intended to be usable to help banks absorb losses in stress, while maintaining the provision of services to the real economy. They do so by reducing incentives for banks to restrict credit supply abruptly and excessively.

Experience and a range of research suggests, however, that banks are reluctant to use their capital buffers in practice. For example, evidence from the Covid period suggests that while cutting the CCyB was effective in supporting lending, banks were less willing to use other non-releasable buffers. In the event of a severe macroeconomic shock, if banks were unwilling to use their buffers and so cut credit supply abruptly, businesses could be unable to meet their financing needs – which could trigger larger corporate losses for banks, deepen the economic stress and have an even greater negative effect on banks' capital ratios.

Furthermore, a desire to avoid using regulatory capital buffers contributes to banks' incentives to maintain capital headroom over regulatory requirements and buffers. There are various reasons why banks choose to have such headroom, including investor and rating agency expectations, business models and strategic plans, regulatory requirements set by overseas regulators, and the need to manage capital volatility. But to the extent that incentives to maintain excess capital can be reduced by enhancing buffer usability, this could allow banks to support a material increase in lending.

The FPC and PRA have already taken a number of steps to enhance buffer usability. The FPC has cut the CCyB to zero on a number of occasions. The FPC and PRA have also emphasised that buffers are usable in a stress and that they do not oblige banks to have capital in excess of regulatory minima and buffer requirements. The reduction of the FPC's important Tier 1 benchmark to 13% should also provide banks with greater certainty and confidence to use their existing capital to support lending to the real economy.

Working with the PRA and international authorities, the FPC will explore further ways to facilitate the use of buffers. The aim of that work will be to meaningfully reduce incentives for banks to: a) deleverage in stress; and b) maintain capital in excess of regulatory requirements and buffers in normal times. For example, further consideration could be given to the ideas introduced in Sam Woods' '**Bufferati**' speech, which sets out a vision for a simpler capital framework, including moving to a single releasable buffer, and replacing automatic distribution restrictions with a ladder of intervention tools operated with supervisory judgment.

> **The FPC will review the implementation of the leverage ratio in the UK, to ensure that it functions as intended. Within this, the Committee intends to prioritise reviewing the UK's approach to regulatory buffers in leverage ratio requirements.**

When the FPC introduced the leverage ratio as a complement to the risk-weighted framework in 2015, it was envisaged that risk-weighted requirements would form the binding constraint for a majority of UK banks most of the time. Over time, however, falls in banks' average risk weights have meant that the leverage ratio has become the binding requirement, or close to the binding requirement, for a greater number of banks. Three out of seven major UK banks' leverage-based minimum requirements and buffers are now the binding Tier 1 regulatory requirement at consolidated level.

While there are reasons for the differences in application of the leverage ratio in the UK and some other countries, including previous macroprudential decisions by the FPC to apply buffers alongside Basel minimum standards, international comparisons also point to some potentially important areas to consider for reform.

As a result, the FPC will review how the leverage ratio has been implemented in the UK, how it is operating in practice, how it is interacting with other policies such as ring-fencing, and whether this matches the original intention of the framework. For example, the FPC will explore the extent to which the leverage ratio has become more binding as a result of underlying reductions in the riskiness of banks' exposures. The Committee intends to prioritise reviewing the UK's approach to regulatory buffers in leverage ratio requirements.

> **The FPC supports initiatives by the Bank to respond to feedback on interactions, proportionality and complexity in the capital framework.**

The FPC supports further work to consider how the capital requirements that are related to domestic exposures interact. Capital requirements that are related to domestic exposures include the UK CCyB, Other systemically important institution (O-SII) buffers, and Pillar 2A requirements for geographic credit concentration risk, which each serve different purposes in the capital framework, but are all calibrated based on measures of domestic lending. The FPC and the PRA intend to draw on several sources of information when conducting this work including on the impact of systemic failures and credit concentration, and banks' stress-test results.

Other initiatives include:

- Further work to develop a systematic approach for updating the regulatory thresholds that define which different parts of the regulatory framework apply to firms, to ensure they reflect economic growth – such as through automatic indexation.
- The PRA's contribution to the Government's review of ring fencing. The Government has made clear its intention to uphold the ring-fencing regime to protect financial stability and safeguard depositors, while at the same time drive meaningful reform of the regime as part of plans to focus on growth and the release of capital for productive investment in the UK. The PRA will also review the application of the Basel 3.1 output floor at the ring-fenced sub-group level, based on evidence and experience of its implementation. It will do so after Basel 3.1 is implemented but before full weighting of the output floor in 2030.
- Reviewing feedback received on the PRA's discussion paper on capital requirements for mortgages under the internal ratings-based approach to reduce barriers to using this approach. This could enable more lenders to use it, and so help to ensure the appropriate channelling of finance to creditworthy households.

The FPC considered industry feedback that earlier loss recognition in the Bank's stress tests under the International Financial Reporting Standard (IFRS) 9 accounting standard could result in an unwarranted increase in capital requirements. In response, the Bank made a set of changes to the stress test that have avoided such an outcome.

This year's Bank Capital Stress Test contained a number of changes relative to previous concurrent stress tests which the Bank judged to be appropriate to make alongside the earlier provisioning that comes with the IFRS 9 accounting standard (Box E). The FPC judges that these changes have been effective in avoiding an unwarranted increase in capital arising from the interaction of IFRS 9 and the stress test, and made the test simpler and aligned with the accounting standard that would apply in an actual stress. The Bank therefore intends to maintain these changes for future tests.

The FPC and PRA are interested in the views of a broad range of stakeholders – including UK lenders, think-tanks, industry groups, investors, and academics – on the material covered in this box and the accompanying Financial Stability in Focus, and welcome feedback and evidence on the issues identified for further assessment.

In early 2026, the Bank intends to organise structured evidence gathering sessions on the topics listed. It is also open to written feedback on these topics, which can be submitted up until 2 April 2026 via ✉ **FPCBankCapitalReview@bankofengland.co.uk**. The FPC intends to provide a further update on this work in the next Financial Stability Report.

5: In focus – Results of the 2025 Bank Capital Stress Test

5.1: Key features of the 2025 Bank Capital Stress Test

The 2025 Bank Capital Stress Test assesses UK banks' ability to support the economy even if economic conditions turn out materially worse than expected.

In line with the Bank's updated **approach to stress testing the UK banking system**, the 2025 Bank Capital Stress Test assesses the resilience of the UK banking system to a hypothetical scenario that includes a severe but plausible combination of macroeconomic and financial shocks. The exercise helps to ensure the UK banking system can continue supporting households and businesses even in a macroeconomic downturn. Stress testing plays an important role in ensuring a stable financial system which supports long-term sustainable growth by helping ensure banks can absorb rather than amplify shocks.

The largest and most systemic UK banks and building societies[14] – representing around 75% of the sector's lending to the UK real economy – participate in the test. They submit their estimates of the impact of the scenario, which is considered together with the Bank's own analysis to produce the final results. The test supports the FPC's and Prudential Regulation Committee's (PRC's) monitoring of the resilience of the banking system, and can be used to inform banking-system wide and individual bank capital-setting.

As set out in this chapter, the results of the test indicate that the banking system has the capacity to continue supporting households and businesses even if economic and financial conditions turned out materially worse than expected.

The 2025 Bank Capital Stress Test scenario is severe but plausible, representing a 'tail-risk' scenario rather than forecasts of macroeconomic and financial conditions.

In March 2025, the Bank published the **Key elements of the 2025 Bank Capital Stress Test** including its approach to calibrating the scenario in the test. Under that approach, shocks to key macroeconomic variables are benchmarked to historical experience and incorporate the FPC's assessment of domestic and global vulnerabilities. This includes countercyclical judgements which increase the size of shocks when vulnerabilities to particular regions or markets have increased and reduce the size of shocks when risks have abated or crystallised.

The stress scenario is not a forecast of macroeconomic and financial conditions. Rather, like previous concurrent stress test scenarios, it is intended to be a coherent 'tail-risk' scenario designed to be severe and broad enough to allow the FPC and PRC to assess the resilience of UK banks to a range of adverse shocks.

The scenario includes a severe global aggregate supply shock, which leads to deep recessions across countries. An escalation of geopolitical tensions leads to a sharp increase in commodity and energy prices. Global trading relationships fragment, leading to severe supply chain disruptions, which contributes to a large fall in world trade volumes. Together these shocks lead to a sharp rise in inflation across advanced economies, with rising costs falling unevenly across households and businesses. Central banks raise interest rates to bring inflation back to target.

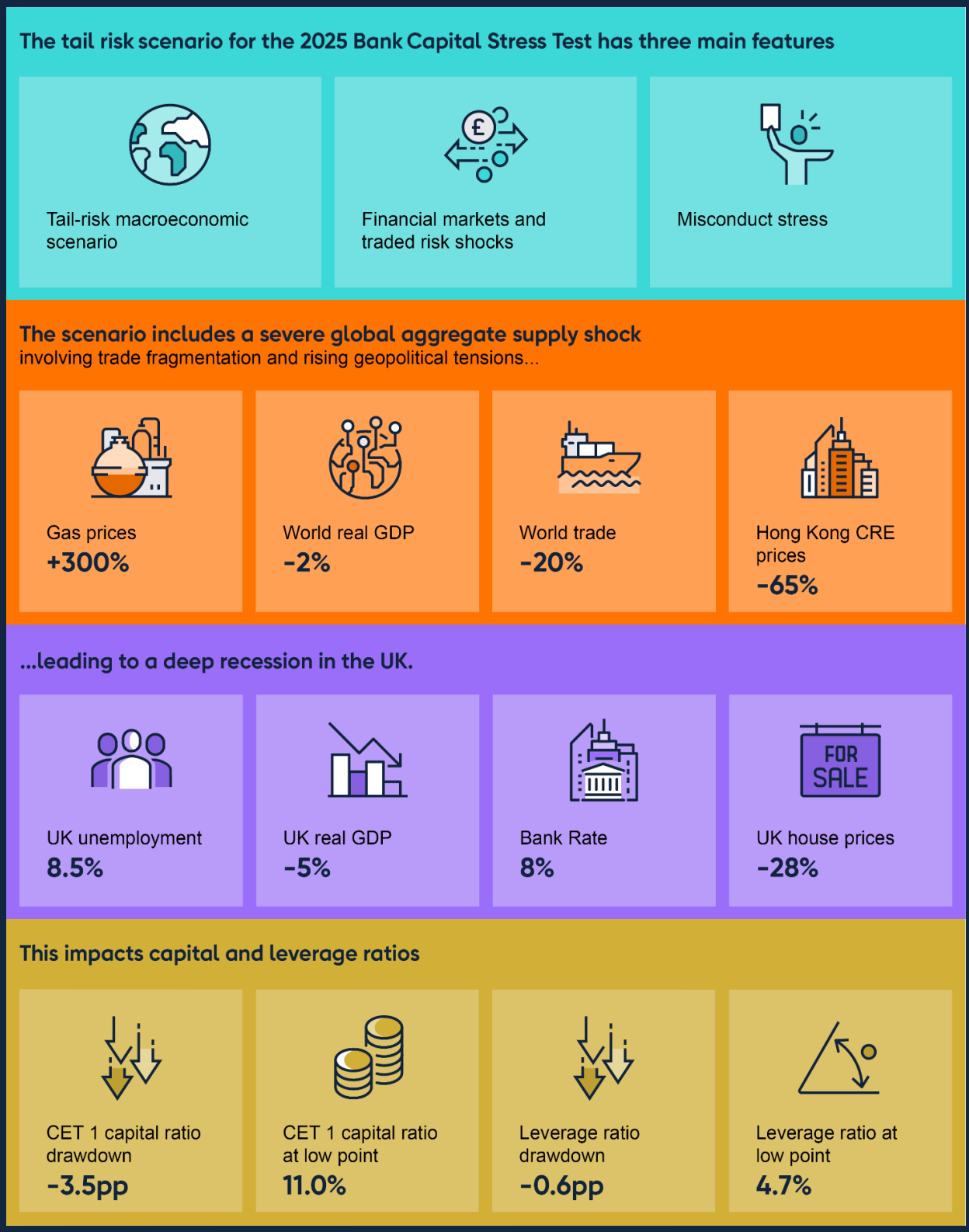
The global aggregate supply shock results in severe recessions in the UK and global economies. UK GDP falls by 5% and unemployment rises to 8.5%. World GDP falls by 2%. UK and global house prices fall sharply in the scenario, and commercial real estate (CRE) prices fall in addition to recently observed price falls. Increased risk aversion leads to large falls in asset prices, while elevated sovereign debt levels in advanced economies put further upward pressure on government bond yields.

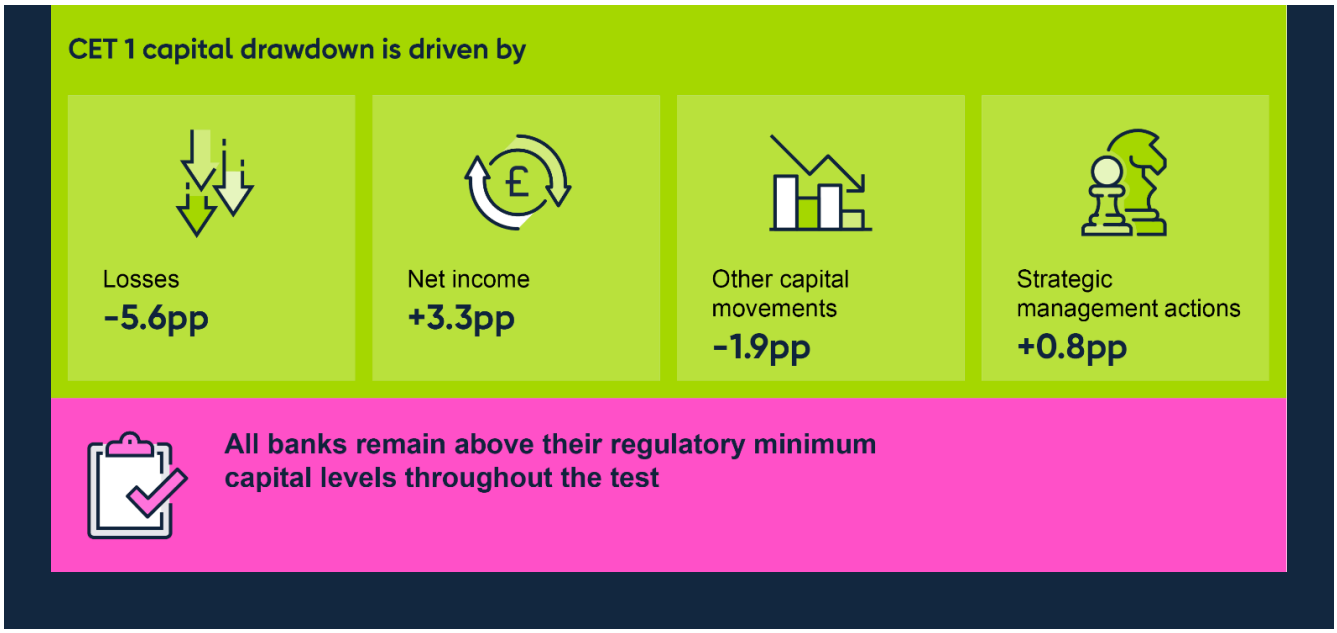
The 2025 Bank Capital Stress Test also includes a financial market stress aligned with the macroeconomic scenario to test trading risks, as well as stressed projections for costs related to known misconduct issues.

> **As part of the test, the FPC assesses whether the banking system has the capacity to support households and businesses throughout the stress.**

Banks must conduct the exercise on the basis that they meet the credit demand of creditworthy UK households and businesses in the stress at a price that is consistent with the overall scenario. Credit growth slows in the early part of the stress reflecting lower credit demand and a worsening economic outlook, however it recovers in the later years and lending to the UK real economy is assumed to increase by more than 6.5% over the scenario horizon. The test results also allow for rising interest rates and decreasing real incomes resulting in competitive pressure in deposit markets which is reflected in higher deposit pricing.

Figure 5.1: Summary of the 2025 Bank Capital Stress Test (a) (b) (c) (d)





Sources: Refinitiv Eikon from LSEG. Participating banks' Stress Test Data Framework (STDF) submissions, Rating and Valuation Department, the Government of the Hong Kong Special Administrative Region Bank and Bank analysis and calculations.

(a) Unemployment rates and Bank Rate are shown as their peak percentage values in the scenario. Other variables are shown as percentage or percentage point changes from the start of the scenario to the peak or trough values for each variable. Except for Hong Kong commercial real estate prices which are shown as percentage changes relative to their peak level in 2018 Q4.
(b) Gas prices defined as UK natural gas prices in pence per therm. The value has been rounded to one significant figure.
(c) World trade defined as the market exchange rate-weighted volume of world imports. Regional import volumes aggregated using the dollar value of imports as a share of the world total.
(d) World real GDP defined as purchasing power parity-weighted world real gross domestic product (chained volume measure).

The results of the Bank Capital Stress Test are informed by both the Bank's and participating banks' estimates of the impact of the scenario…

Modelling and analysis by participating banks provides an in-depth view of each bank's resilience to stress, while supporting a continued improvement in banks' own risk management and capital planning capabilities. Modelling and analysis performed within the Bank allows banking system comparisons and benchmarking across peers, helping ensure consistency in the overall results of the test. Considering participating banks' projections alongside those of the Bank allows the Bank to establish informed judgements about what would happen if the stress were to materialise by incorporating a range of analytical perspectives. These judgements informed adjustments made to the participating banks' submitted projections.

As in previous tests and as per the **Guidance on the 2025 stress test for participants**, participating banks submit the management actions they consider they would undertake in the scenario, such as reducing their dividend payments, reducing variable remuneration (such as bonuses) and cutting costs. The Bank considers each proposed management action in the stress individually, including how realistic the action is in the context of the scenario. For example, any action proposed must be executable in practice with no material impediments envisaged. Unless otherwise specified, banks' results incorporate the application of those management actions judged acceptable by the Bank.

The 2025 Bank Capital Stress Test is the first exercise involving bank submissions of stressed projections since the 2022/23 Annual Cyclical Scenario (ACS) test, therefore most comparisons in this chapter are made to that exercise.[15]

…and are supported by sensitivity analysis.

Testing the impact of different assumptions and a crystallisation of different risks is an important feature of the Bank's **updated approach to stress testing**. This can be an important tool in enhancing insights given the inherent degree of uncertainty around the results of stress tests.

Sensitivity analysis considers the impact on bank resilience of changing the macroeconomic scenario variables or the key assumptions within an exercise. In the 2025 Bank Capital Stress Test this includes sensitivity analysis which assesses the impact of more severe declines in UK house prices and different assumptions about net interest income (NII).

This year the Bank has made changes to the stress-testing framework that have made the stress test simpler to deliver and ensure that the resilience that comes with earlier provisioning under IFRS 9 is recognised. The FPC judges that the changes are consistent with an unchanged risk tolerance for the resilience of the UK banking system.

On 1 January 2018, major UK banks implemented the IFRS 9 accounting standard (Box E). Under IFRS 9, banks set aside provisions for expected credit losses on all loans – not just loans that are past due or already in default. Banks are therefore expected to set aside provisions to cover credit losses earlier than under the previous accounting standard. All else equal, the earlier recognition of losses in a stress under IFRS 9 leads to sharper capital drawdowns in the early part of the stress test. Temporary measures have been used to manage the capital impacts of using IFRS 9 in past stress tests while an enduring solution was identified.

This year the Bank has made changes to its framework that enabled the stress test to be simpler to deliver and ensured that the resilience associated with earlier provisioning is recognised, consistent with the intention of IFRS 9. The FPC judges that the net impact of changes to the stress testing framework and IFRS 9 have avoided an unwarranted increase in capital requirements and are consistent with an unchanged risk tolerance for the resilience of the UK banking system.

The Bank previously set out its intention to use the 2025 Bank Capital Stress Test to assess the impact of the framework changes and IFRS 9 to inform the appropriate benchmark against which to assess banks in future stress tests. Given this intention, and as indicated in March, bank-specific low points in the scenario have been published alongside minimum requirements (in Annex 2). All banks also remain above the sum of their minimum requirements and systemic risk buffer throughout the stress scenario.

In line with international standards, and consistent with the framework set in 2018 by the FPC, systemic banks should be expected to withstand a stress that is more severe than non-systemic banks, which is reflected in systemic risk buffers. As such, in future stress tests the Bank expects to

return to assessing the resilience of individual banks against the sum of minimum capital requirements and systemic risk buffers. Systemic risk buffers would be, like all other capital buffers, useable to absorb losses in a real stress.

5.2: Overview of results of the test

The results of the 2025 Bank Capital Stress Test show that the UK banking system could continue to support the economy, even if economic and financial conditions turned out materially worse than expected.

The banking system starts the test in a strong capital position, with a Common Equity Tier 1 (CET1) capital ratio of 14.5% in aggregate. The aggregate CET1 capital ratio falls to a low point of 11.0% in the first year of the stress, which equates to an aggregate capital drawdown of 3.5 percentage points. The aggregate Tier 1 leverage ratio starts at 5.3%. It falls to a low point of 4.7% in the first year of the scenario.

At the low point, capital remains around £60 billion above the sum of aggregate minima and systemic buffers, indicating that the UK banking system would be resilient to the severe but plausible scenario and would have the capacity to continue lending to creditworthy households and businesses throughout the stress.

Most of this headroom arose from banks beginning the test with capital in excess of regulatory requirements.

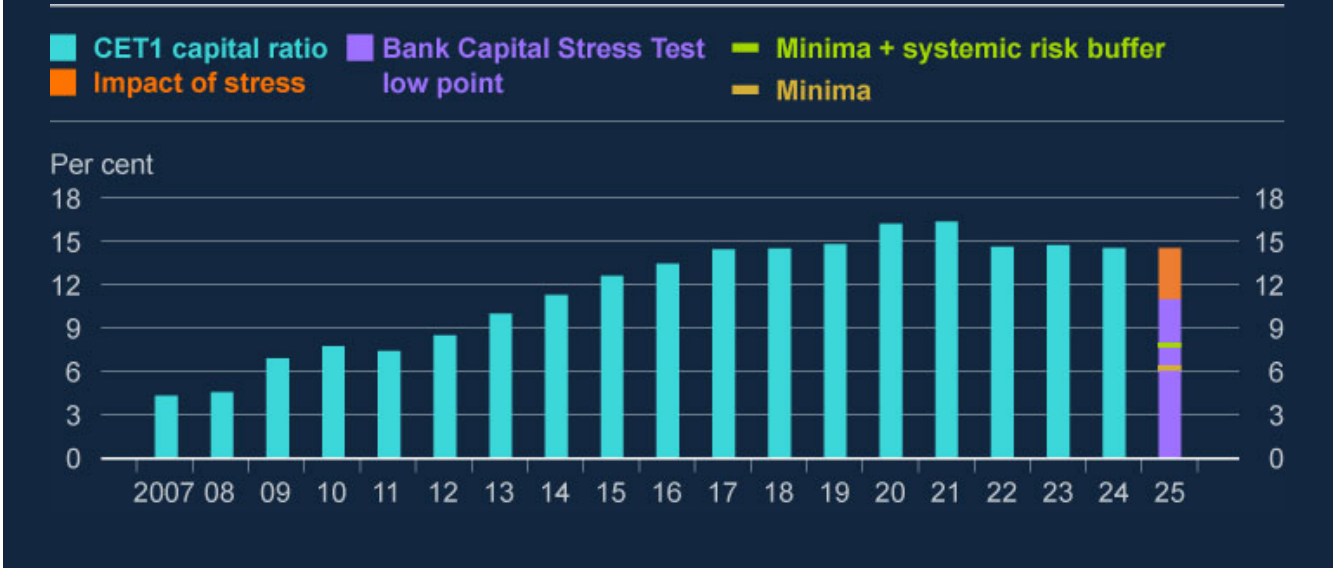
Around £45 billion of the aggregate headroom to regulatory minima and systemic buffers at the low point of the test arises from banks beginning the test with significant headroom over starting regulatory minima and buffer requirements. There are a number of reasons why banks maintain capital in excess of regulatory requirements, including varying business models and strategic plans.

The FPC has noted as part of its capital review that there are impediments to banks using their buffers in practice, which may be also contributing to banks' incentives to maintain capital in excess of regulatory requirements. For example, evidence from Covid suggests that while cutting the countercyclical capital buffer, a buffer that the FPC can take action to release in stress, was effective in supporting lending, banks were less willing to use other non-releasable buffers.

The FPC and PRC do not oblige banks to maintain buffers in excess of regulatory requirements. All elements of capital buffers that have been built up by banks exist to be used to support households and businesses during stress. The existence of usable buffers allows banks to absorb losses without breaching minimum requirements, enabling them to meet the demand for credit from creditworthy households and businesses in the face of severe adverse shocks. As part of the next phase of its capital review (Box D), the FPC will explore further steps that can be taken to enhance the usability of buffers.

Chart 5.1: The UK banking system is resilient to support the economy, with the aggregate capital ratio remaining well above minima at the low point of the stress test scenario

Aggregate CET1 capital ratio and impact of the 2025 Bank Capital Stress Test scenario (a)



Sources: PRA regulatory returns, published accounts, STDF and Bank analysis and calculations.

(a) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the Capital Requirements Regulation (CRR).

No individual bank is required to strengthen its capital position as a result of the test.

The results of the test indicate that no individual bank would fall below its CET1 capital or Tier 1 leverage ratio minima (Table 5.A).[16] This means that major UK banks would be able to withstand the severe macroeconomic stress in this scenario, while still having the capacity to support UK households and businesses throughout the stress. All banks would also have remained above the sum of their regulatory minima and systemic risk buffers, which is the hurdle rate the Bank expects to return to using in future tests.

Table 5.A: All banks remain above their CET1 capital ratio and Tier 1 leverage ratio minima

Bank-level results of the 2025 Bank Capital Stress Test (a) (b) (c) (d) (e) (f) (g) (h)

	CET1 capital ratio			Leverage ratio		
	Start point	Low point	Minima	Start point	Low point	Minima
Barclays	13.5%	9.3%	7.2%	5.0%	4.2%	3.3%
HSBC	14.9%	11.9%	5.8%	5.6%	5.1%	3.3%
Lloyds	14.2%	10.9%	5.9%	5.5%	4.6%	3.3%
Nationwide	19.5%	14.5%	6.5%	5.2%	4.8%	3.3%
NatWest	13.6%	11.1%	6.0%	5.0%	4.7%	3.3%
San UK	14.8%	10.3%	6.9%	4.9%	3.9%	3.3%
Standard Chartered	14.2%	9.8%	6.1%	4.8%	4.6%	3.3%
Aggregate	**14.5%**	**11.0%**	**6.2%**	**5.3%**	**4.7%**	**3.3%**

Sources: STDF and Bank analysis and calculations.

(a) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets (RWAs)), where CET1 capital and RWAs are determined in accordance with the CRR.
(b) Tier 1 capital is defined as the sum of CET1 capital and Additional Tier 1 capital determined in accordance with the CRR.
(c) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a bank does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by PRA rules), Additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(d) Minimum aggregate CET1 capital ratios are calculated by dividing aggregate CET1 capital by aggregate RWAs at the aggregate low point of the stress in 2025. Minimum aggregate Tier 1 leverage ratios are calculated by dividing aggregate Tier 1 capital by the aggregate leverage exposure measure at the aggregate low point of the stress in 2025.
(e) The minimum CET1 capital ratios and leverage ratios shown in the table do not necessarily occur in the same year of the stress scenario for all banks. For individual banks, low-point years are based on their positions after any strategic management actions and automatic distribution restrictions.
(f) Low points for CET1 capital and Tier 1 leverage ratios occur in year 2 for Santander UK and year 1 for all other banks.
(g) The aggregate minima is calculated as a weighted average of minima in the aggregate low-point year.
(h) To produce aggregate results in a single currency, the Bank converts the results of HSBC and Standard Chartered – which report in US dollars – into sterling at a rate consistent with the scenario.

The stress affects capital positions through several channels, notably credit impairments and net interest income.

Table 5.B decomposes the change in the aggregate CET1 capital ratio and leverage ratio between the start point (end-December 2024) and the low point (the following year, or ‘year 1’) into each of its constituent components.

The key drivers of the capital drawdown are an increase in credit impairments (Section 5.3) and traded risk losses (Section 5.4), which are only partially offset by higher NII in the first year of the stress (Section 5.5). Other factors that drive the results include changes in RWAs, operating expenses, other profit and loss (P&L) statement items, misconduct costs and assumptions about strategic management actions (Section 5.6).

Table 5.B: Credit impairments and traded risk are key drivers of lower capital ratios in the stress

Contributions to the changes in the aggregate CET1 capital ratio and Tier 1 leverage ratio between the start and low points of the 2025 Bank Capital Stress Test (percentage points, unless otherwise stated) (a)

Line item	CET1 capital ratio	Leverage ratio
Start point (Year 0)	**14.5%**	**5.3%**
Net interest income	5.1pp	1.5pp
Net fees and commission income	1.3pp	0.4pp
Net traded income	1.1pp	0.3pp
Operational expenses	-4.2pp	-1.3pp
Net income less expenses	**3.3pp**	**1.0pp**
Impairments	-3.3pp	-1.0pp
Traded risk losses	-2.0pp	-0.6pp
Misconduct	-0.3pp	-0.1pp
Operational risk	-0.1pp	0.0pp
Losses	**-5.6pp**	**-1.7pp**
RWAs/Leverage exposure	-1.1pp	0.1pp
Tax and other P&L and capital	-0.4pp	-0.1pp
Distributions	-0.4pp	-0.1pp
RWAs and other capital items	**-1.9pp**	**-0.2pp**
Drawdown pre-SMA (Year 1)	**-4.3pp**	**-0.9pp**
SMAs	0.8pp	0.3pp
Drawdown post-SMA (Year 1)	**-3.5pp**	**-0.6pp**
Stress test low-point (Year 1)	**11.0%**	**4.7%**
Minima	**6.2%**	**3.3%**
Minima and Systemic Risk Buffer	**7.8%**	**3.8%**

Sources: STDF and Bank analysis and calculations.

(a) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the Capital Requirements Regulation (CRR).

5.3: Credit impairments

Banks incur credit impairments of £112 billion over the test.

Credit impairments are the main driver of capital depletion in this stress scenario. Higher unemployment and lower corporate profits reduce households' and corporates' ability to repay their loans, and lower property prices affect underlying residential and commercial property collateral value. High interest rates lead to affordability pressures, and vulnerable sectors are affected by a steep increase in energy prices and global trade fragmentation.

Credit impairments reduce the aggregate CET1 capital ratio by 3.3 percentage points at the low point (year 1). Impairments over the five years of the stress scenario total £112 billion, with an aggregate impairment rate of 3.3%. The impact of RWA changes is covered in Section 5.6.

Table 5.C provides a breakdown of these impairments by asset class. This section explains the key drivers, and where they differ from the 2022/23 test (which had £125 billion of impairments and an overall impairment rate of 3.9%).

Table 5.C: Impairments are estimated at £112 billion over the five years of the Bank Capital Stress Test

Aggregate cumulative impairment charges and rates over the five years of the stress (a) (b)

	2025 Bank Capital Stress Test		2022/23 ACS	
Lending portfolio	**Impairment charge**	**Rate**	**Impairment charge**	**Rate**
UK: lending to business	£22.6 billion	8.6%	£21.6 billion	8.3%
of which leveraged lending	£3.0 billion	n.a.	£2.4 billion	n.a.
UK: lending to individuals	£41.5 billion	2.9%	£41.4 billion	3.0%
of which UK consumer credit	£29.3 billion	23.3%	£29.8 billion	27.2%
of which UK mortgages	£12.3 billion	1.0%	£11.6 billion	0.9%
Total UK	**£64.1 billion**	**3.8%**	**£63.1 billion**	**3.9%**
Non-UK: lending to business	£23.8 billion	5.4%	£33.3 billion	5.9%
of which leveraged lending	£5.1 billion	n.a.	£6.7 billion	n.a.
Non-UK: lending to individuals	£20.8 billion	6.5%	£23.2 billion	6.3%
Total non-UK	**£44.6 billion**	**5.8%**	**£56.5 billion**	**6.1%**

Sources: STDF and Bank analysis and calculations.

(a) Cumulative impairment charge rates are calculated as the five-year total impairment charge divided by average gross on-balance sheet exposures.
(b) Other wholesale lending is excluded in Table 5.C. Other wholesale lending consists of lending to financial institutions, housing associations, sovereigns, quasi-sovereigns and other wholesale counterparties.

Retail impairments increase as unemployment rises, house prices fall, and interest rates and the cost-of-living increase.

The impact of the stress on UK retail portfolios is similar to that in the 2022/23 ACS, reflecting several offsetting factors. There is a reduced impact from the affordability stress in this exercise reflecting the improvement in the underlying outlook for real incomes.[17] This is offset by deteriorating asset quality.

- **UK mortgage impairments** are £12.3 billion which is higher than in the 2022/23 ACS. Asset quality has deteriorated since the 2022/23 ACS as higher interest rates have increased debt servicing costs, while house prices have remained stable. This has pushed average loan to value (LTV) ratios higher, reducing the value of collateral against loans, which increases the loss when a loan defaults. The impairment rate for buy-to-let (BTL) mortgages is almost three times that of owner-occupied mortgages.

- **UK consumer credit impairments** are £29.3 billion which is lower than in the 2022/23 ACS. As set out in Box E, the Bank has reviewed past judgements and recent evidence on consumer credit quality and has allowed for lower consumer credit loss rates in the 2025 Bank Capital Stress Test than in past exercises. The less severe inflation path in this test has also reduced the affordability impact. However, the impact of lower loss rates is offset by larger consumer credit balances meaning impairment charges are comparable to that in the 2022/23 ACS.
- **Non-UK consumer credit impairments** are £19 billion, which is lower than in the 2022/23 ACS. This is due to improved asset quality in non-UK consumer lending which includes a range of countries and products.

Corporate impairments increase as GDP, corporate profits and CRE prices fall. Rising costs, trade disruption and higher interest rates impact vulnerable sectors.

There are common drivers of impairments across corporate portfolios – for example 70% of banks reported impairments were from sectors judged vulnerable to rising costs, trade disruption and higher interest rates. These include manufacturing, real estate and construction.

- **UK corporate impairments** totalled £22.6 billion. This is slightly higher than in the 2022/23 ACS as improvements in asset quality were offset by larger corporate exposures. UK CRE impairment rates are broadly unchanged since the 2022/23 ACS, as price falls over the previous 18 months have contributed to increased LTV ratios. These price falls are also reflected in lower start-to-trough falls in UK CRE prices as part of the countercyclical scenario which offsets the impact.
- **Non-UK corporate impairments** totalled £23.8 billion. This is significantly lower than in the 2022/23 ACS, primarily driven by a reduction in CRE losses in Hong Kong and China. The period since the last ACS has seen a significant crystallisation of losses against which banks have set aside substantial provisions (£6.4 billion). While material risks remain in the sector, the worst quality assets have been written off, and the remaining total exposure is reduced by about 40%. Start-to-trough price falls are also smaller than the 2022/23 ACS, consistent with the countercyclical approach to the scenario.

The results of the test continue to include banks' exposures to leveraged lending.

The five-year impairment rate across all leveraged lending exposures was 13%, compared to less than 8% in the global financial crisis (GFC). This reflects relative asset quality and vulnerability to a larger interest rate shock. Corporates are assumed to increase their usage of revolving credit facilities – at a drawdown rate of 80% – throughout the five-year scenario. This reflects ongoing uncertainty as to the behaviour of financial sponsors in a severe downturn.

Sensitivity analysis suggests that increasing the severity of house price falls could have a non-linear impact on credit losses.

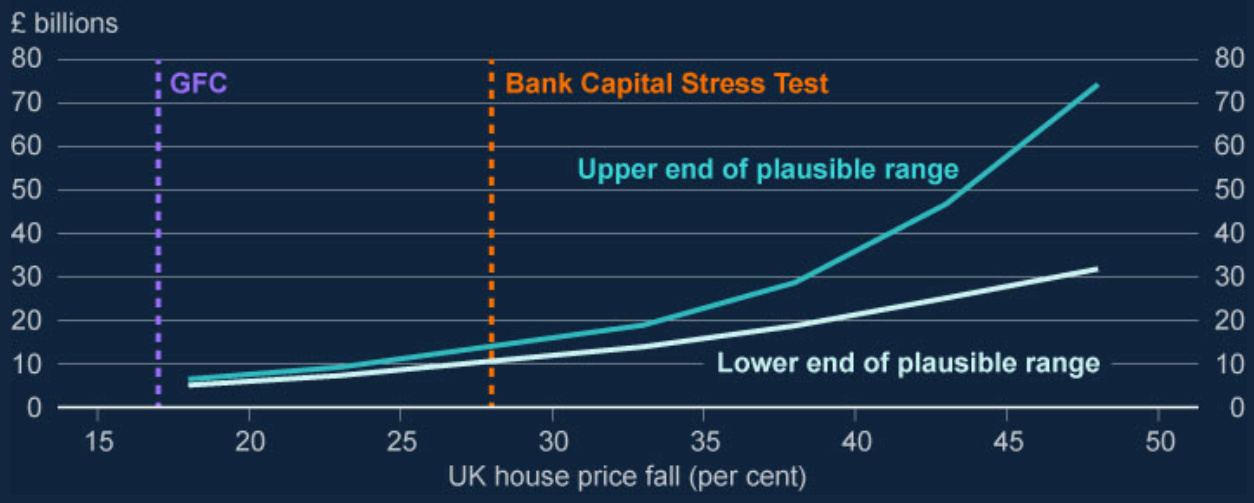
Sensitivity analysis can be used to explore the impact of including more severe UK house price falls in the scenario. Such analysis suggests that increasing the size of the house price shock would have a non-linear impact on UK mortgage impairments. This reflects the fact that a large

majority of UK mortgages on banks' books currently have an LTV ratio of below 70%.

Chart 5.2 shows that increasing the UK house price fall beyond 30% would tend to have an increasing marginal impact on bank losses as a greater proportion of their lending would be secured on collateral worth less than the value of the loan. For instance, if the fall in UK house prices were 10 percentage points greater, aggregate UK mortgage impairments would be around twice as great as in the Bank Capital Stress Test. Such large declines in property prices, in nominal terms, would be significantly beyond those historically experienced in the UK.

Chart 5.2: Sensitivity analysis suggests increasing the size of the UK house price shock would have a non-linear impact on credit losses

UK mortgage impairments at different house price shocks



Sources: ONS, STDF and Bank analysis and calculations.

5.4: Traded risk

The traded risk scenario reduces banks' aggregate CET1 capital ratio by 0.8 percentage points in the first year of the stress.

The scenario leads to losses for banks through traded risks and investment banking via three main channels: trading book stress losses, valuation adjustments, and lower investment banking income.

In the traded risk scenario, global equity prices decline sharply, with the FTSE All-Share index falling by 48%, and the S&P 500 falling 57%. Measures of market-implied volatility also rise, with the Chicago Board Options Exchange Volatility Index (VIX) increasing to a peak of 45. Corporate bond spreads widen to GFC-era peaks. Against a backdrop of elevated sovereign debt and rising central bank interest rates, government bond yields and term premia increase, and government bond yield spread over overnight indexed swap (OIS) rates widen. The 10-year UK government bond yield increases by 210 basis points at its peak.

Overall, the net impact of these factors reduces banks' capital by around £15 billion, equivalent to 0.8 percentage points of the CET1 capital ratio. Banks generate £20 billion of revenues from investment banking activities, which include primarily market making activities and advisory fees. Revenues decline in the first year of the stress, driven by a sharp fall in fees from advisory activities, though they are somewhat supported by resilient client trading activities in response to increased financial market volatility. However, this revenue is offset by £35 billion of losses due to the stress scenario leading to losses in fair-value through other comprehensive income securities, trading inventories and related valuations adjustments. Higher interest rates and a higher spread between government bond yields and OIS rates in the scenario lead to lower fair value of bond holdings in banks' liquid asset buffers, which contributed to a £15.5 billion reduction in capital. Trading book losses from market risk shocks, defaults of selected vulnerable counterparties and valuation adjustments contributed to a £19 billion reduction in capital, reflecting the sudden and severe shocks to financial markets.

5.5: Net interest income

Net interest income is an important driver of the results.

NII is the difference between what banks earn on their assets and what they pay on their funding. It is an important source of income for banks and a means through which they can rebuild capital resilience and their capacity to support households and businesses through a stress.

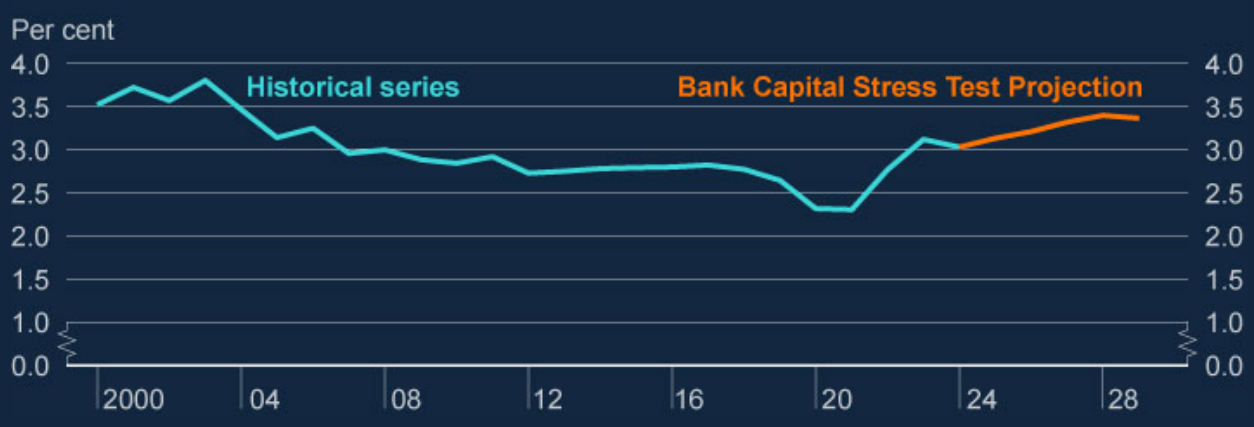
Banks' loan margin, calculated as NII divided by total lending, is affected by both the asset spread and the deposit spread to risk-free reference rates. It is also driven by banks' ability to invest non-interest-bearing liabilities and equity in fixed-interest bearing assets referred to as structural hedge portfolios. These structural hedge portfolios – which often include interest rate swaps – stabilise income through the interest rate cycle, slowing the costs of falling interest rates and the benefits from rising interest rates.

NII increases over the stress.

Over recent years, as interest rates increased from historically low levels, loan margins recovered to be in line with historical averages (Chart 5.3). As such, the starting level of NII is higher than it was for the 2022/23 ACS, particularly on non-UK portfolios.

Chart 5.3: Loan margins rise over the stress scenario

Loan margin in the 2025 Bank Capital Stress Test (a) (b)



Sources: STDF and Bank analysis and calculations.

(a) Loan margin is calculated as net interest income divided by total lending. Loan margins in this chart are calculated across all currencies. Net interest income is interest income minus interest expense.
(b) Figures between 2000 and 2019 exclude Virgin Money UK, and figures before 2006 exclude Standard Chartered.

In the scenario, banks continue to support the UK economy through their deposit and loan pricing.

Judgements about banks' pricing have been taken to test banks' ability to continue supporting UK households and businesses in the stress scenario. These judgements allow for competitive pressure arising from savers and borrowers - as interest rates increase and real incomes decrease in an economic downturn - to be reflected in the results. They also ensure a level of market-wide consistency. Taking all of these together, net interest income rises over the scenario, but remains within the range of historical experience (Chart 5.3).

First, it is assumed that spreads on lending to UK households and businesses increase by only a limited amount that reflects higher expected credit losses on new loans. For example, spreads between mortgage rates and risk-free interest rates are assumed to widen only to around 80 basis points in the test, compared to around 60 basis points at the start of the stress scenario.

Second, as interest rates increase many customers would move deposits from accounts that pay no interest to deposit accounts that do pay interest. In aggregate the share of deposit balances that are non-interest bearing is assumed to decline over the five years of the scenario and ends 15 percentage points below its peak, at a similar level to that seen prior to the GFC.

Third, it is assumed that banks pass through around 70% of the increase in Bank Rate to sterling deposit rates within the first year of the stress. This is a greater and faster level of pass through than the experience of the full recent tightening cycle, though this included a re-widening of deposit

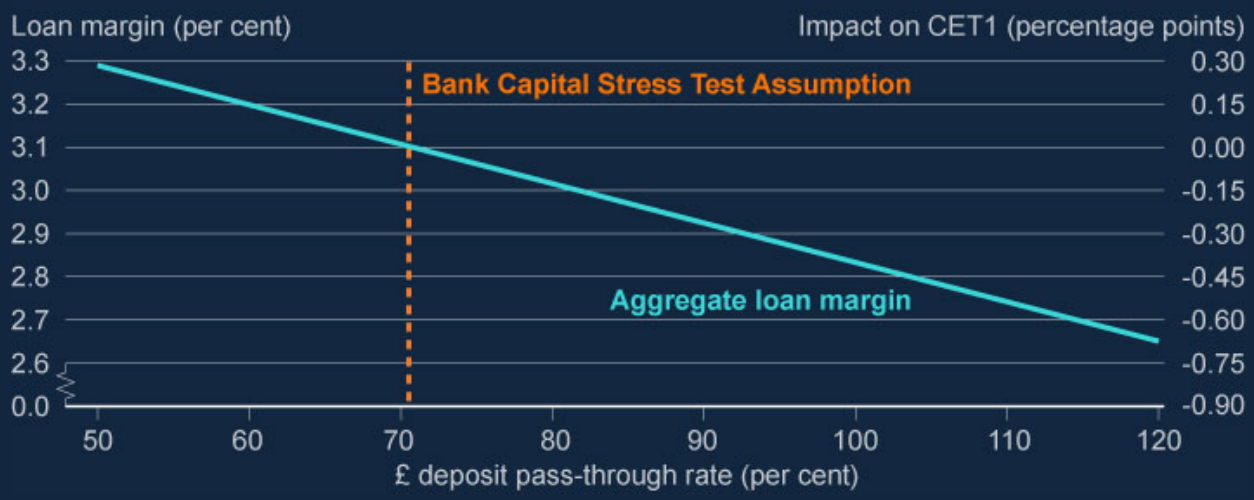
spreads as Bank Rate moved away from the zero lower bound. It is somewhat less than the 80%–90% pass through in the later stages of that cycle, though this estimate may also include some impact from earlier increases continuing to pass-through.

The Bank has used sensitivity analysis to assess how changes in pass-through to deposit rates would impact banks' NII.

There is a range of factors that determine the degree and pace of pass-through from changes in Bank Rate to changes in deposit rates. That includes to what extent, and how quickly, the return on banks' assets adjusts, the degree of competition in deposit markets and banks' funding needs. Sensitivity analysis suggests that a 10 percentage point change in the deposit pass-through rate on sterling deposits would be expected to affect the aggregate CET1 capital ratio by around 15 basis points at the low point of the stress in year 1 (Chart 5.4). This estimated impact of a change in the sterling deposit pass-through rate on the CET1 capital ratio is larger for banks with a greater share of UK-based deposits.

Chart 5.4: Changes in the assumed sterling deposit pass-through rate would impact the aggregate CET1 capital ratio

Annual impact on loan margin and CET1 capital ratio from changes to sterling deposit pass-through rate (a)



Sources: Bank of England, STDF and Bank analysis and calculations.

(a) To produce aggregate results in a single currency, the Bank converts the results of HSBC and Standard Chartered – which report in US dollars – into sterling at a rate consistent with the scenario.

5.6: Other net income, losses and capital items

Risk-weighted assets

Banks' exposures become riskier in stress and average risk weights for credit exposures increase in the scenario. In the first year of the stress, average risk weights for credit exposures increase from 33% to 37%, as these exposures become riskier during the stress. Stressed traded risk also causes RWAs to increase, reflecting counterparty credit risk, market risk and credit valuation adjustment risk.

The increase in risk-weights puts downward pressure on CET1 capital ratios – defined as CET1 capital as a percentage of RWAs – and they fall as RWAs increase.

Operating expenses

Banks enter the stress with higher operating expenses than at the start of the 2022/23 ACS. Increases in commodity prices and supply chain shocks drive up inflation globally in the scenario which increases costs for banks. This is to some extent mitigated in the early years of the scenario by banks having fixed-term contracts and pay deals in place, cost-saving programs already underway, and their ability to reduce variable pay as their profitability falls. Expenses increase materially in later years, as the effect of higher consumer prices feeds through to a rise in staff and non-staff costs. In aggregate, costs increase by 8% over the scenario, compared to a 23% increase in UK consumer prices over the same period.

Misconduct costs

As set out in **Key elements of the 2025 Bank Capital Stress Test**, the stress test includes stressed projections for misconduct costs – beyond those paid or provided for by December 2024 – that relate to known misconduct issues for which a stressed projection with a low likelihood of being exceeded can be estimated. In the 2025 stress test, the aggregate stressed projection for misconduct costs is £13.6 billion over the five years of the stress, with around £4.5 billion of these realised in the first year.

5.7: Management actions

Banks take management actions in the stress to support their capital position.

Such actions must meet criteria set out by the Bank in the **Guidance on the 2025 stress test for participants**. These include 'business-as-usual management actions', which represent decisions taken within banks' business lines in the usual course of managing economic conditions. The other type of management actions are strategic management actions (SMAs), defined as extraordinary actions taken in response to the stress scenario.

As in previous stress tests, banks' resilience relies in part on their ability in a stress to cancel ordinary dividend payments, employee variable remuneration, and coupon payments on Additional Tier 1 instruments, as well as other management actions taken in response to the stress. Banks

are assumed to stop their share buy-back programmes after the first quarter in year 1 of the stress. Banks are able to propose other management actions outside those relating to distributions, consistent with the guidance set out by the Bank.

The FPC judges it important for investors to be aware that banks would take such actions as necessary if such a stress were to materialise. In the 2025 stress test, SMAs support the aggregate CET1 capital ratio by 0.8 percentage points and the aggregate leverage ratio by 0.3 percentage points.

5.8: Uses of the findings of the 2025 stress test

> **The Bank Capital Stress Test plays an important role in supporting long term sustainable growth by testing whether banks can absorb rather than amplify shocks.**

The results of a Bank Capital Stress Test allow an assessment of whether the banking system and individual banks are sufficiently capitalised to be able to continue supporting households and businesses even in a macroeconomic downturn.

As such, it supports both the FPC and the PRA in meeting their statutory objectives for macroprudential and microprudential policy.

> **The FPC and PRC use the results of the Bank Capital Stress Test, along with other relevant information, to help inform the setting of banks' regulatory capital buffers.**

In setting the UK countercyclical capital buffer rate, the FPC takes into account the extent of financial vulnerabilities and the risk that the banking system could experience losses on its UK exposures arising from those vulnerabilities that may result in a restriction in credit supply that is not warranted by the macroeconomic outlook.

The PRC sets individual banks' additional PRA buffers which some banks are expected to maintain in addition to the combined capital buffer – the results of the stress test are one input into the **PRC's decisions on PRA buffers**.

The results of the Bank Capital Stress Test have also been taken into account in the FPC's assessment of the structural level of bank capital requirements, as set out in Box D.

> **The Bank has undertaken a qualitative review of banks' stress-testing capabilities, as in previous years.**

This year the review found continued improvements in the quality of data provided and analysis across a number of areas. The Bank will use formal feedback to engage with banks where it has identified that further improvements can be made.

Box E: Incorporation of the IFRS 9 accounting standard into the stress test

IFRS 9 was introduced in 2018 in part to increase transparency in measures of banks' capital positions through the earlier recognition of credit losses in banks' provisioning, addressing a key lesson learned from the global financial crisis (GFC).

On 1 January 2018, major UK banks implemented the IFRS 9 accounting standard. Under IFRS 9, banks set aside provisions for expected credit losses on all loans – not just loans that are past due or already in default. This means banks are expected to set aside provisions to cover credit losses earlier than under the previous accounting standard.

The earlier recognition of losses under IFRS 9 enhances transparency and market confidence in measures of banks' capital positions, including in a downturn, thereby supporting financial stability and the safety and soundness of individual banks. IFRS 9 reduces the risk of banks being under-provisioned for losses that occur later in a stress.

All else equal, the earlier recognition of losses in a stress under IFRS 9 leads to sharper capital drawdowns in the early part of the stress test than under the previous accounting standard.

The change in accounting standard does not change the cumulative losses banks incur during any given stress episode. The losses will, however, be provided for earlier in the stress. All else equal, bank capital, as measured under IFRS 9, is likely to fall more sharply in the early part of a stress as capital is drawn down earlier to raise provisions.

The results of a Bank Capital Stress Test allow an assessment of whether the banking system and individual banks are sufficiently capitalised and have adequate regulatory capital buffers to be able to absorb losses in the stress scenario, and continue to provide essential services to the real economy. The results of a stress test are one input – alongside a range of other factors – to inform the setting of system-wide and individual bank capital buffers, such as the countercyclical capital buffer (CCyB) and the PRA buffer respectively. [18] By default, the earlier recognition of losses under IFRS 9 would mean that capital buffers implied by the stress test would need to be larger to withstand the same stress scenario.

In 2018, the FPC announced that it would seek an enduring treatment for IFRS 9 in the stress test that avoided an unwarranted increase in capital requirements.

In previous stress tests following the introduction of IFRS 9, temporary measures were used to manage the capital impacts of using IFRS 9 while an enduring solution was identified. Internationally agreed arrangements were put in place to offer banks transitional relief – allowing banks to 'add back' to Common Equity Tier 1 (CET1) capital – as they adapted to the new accounting standard. These transitional arrangements expired on 31 December

2024. Additionally, between 2018 and 2023, the Bank adjusted hurdle rates – the level of capital that banks are expected to maintain in the stress scenario – to take into account the impact of the IFRS 9 accounting standard. These hurdle rate adjustments were intended to be temporary and were complex to implement.

As set out in the **Key elements of the 2025 Bank Capital Stress Test**, the Bank does not consider it appropriate to deliver the enduring treatment for IFRS 9 through changes to the capital framework. This includes the proposal to adjust minimum capital requirements (outlined in the **December 2019 Financial Stability Report**), as well as the potential for a permanent corresponding change in CET1 capital to offset the impact of IFRS 9. To varying degrees, these options would be complex to implement, inconsistent with the intended purposes of IFRS 9, or inconsistent with Basel capital standards.

The Bank has sought to follow three guiding principles as it incorporates IFRS 9 into the Bank Capital Stress Test in an enduring way:

- The stress test should embody a risk tolerance consistent with previous concurrent stress tests. This includes both avoiding an unwarranted increase in capital requirements and continuing to hold systemic banks to a higher standard than non-systemic banks.
- The test should reflect how banks' capital positions would unfold in a real stress and be implemented in a practical way.
- The incorporation of IFRS 9 into the stress test should be transparent and compliant with international standards.

> **This year the Bank has made changes to the stress-testing framework that have made the stress test simpler to deliver and ensure that the resilience that comes with earlier provisioning is recognised, consistent with the intention underlying IFRS 9.**

In the **Key elements of the 2025 Bank Capital Stress Test**, the Bank set out its updated approach to stress-test calibration and PRA buffer setting.[19] This has resulted in a number of changes relative to previous concurrent stress tests, which the Bank has judged to be appropriate to make alongside the earlier provisioning under the IFRS 9 accounting standard:

- To reflect the impact of IFRS 9 when setting the PRA buffer, the Bank will assume a CCyB rate that reflects the FPC's judgement that it would set the neutral rate for the UK CCyB around 2%.[20] This has created space for a greater capital drawdown in the stress scenario before a buffer over and above the CCyB and capital conservation buffer (CCoB) would be needed. In aggregate, this additional drawdown is worth around 0.5 percentage points of CET1 capital, taking into account each bank's proportion of UK exposures in its risk-weighted assets. The setting of the PRA buffer will not vary mechanically with changes in the CCyB rate.[21]

- The Bank reviewed the timing and transmission of shocks in the stress scenario, delaying the timing of the peaks and troughs of key macroeconomic variables such as unemployment, real GDP and property prices. This has resulted in a scenario that is more closely aligned to the average of historical advanced-economy stresses and the GFC and has led to some credit losses being recognised later in the exercise. This change has contributed to a reduction in the aggregate proportion of five-year losses in the first year of the stress scenario from 59% in the 2022/23 Annual Cyclical Scenario to 52% in the 2025 Bank Capital Stress Test.
- The approach to setting the size of shocks in the scenario has been updated to incorporate additional data to ensure consistency with historical experience and to simplify the methodology. This updated methodology has resulted in the start-to-trough changes in some variables being somewhat smaller over the scenario horizon than they otherwise would have been. Based on the Bank's estimates, the impact on the aggregate capital drawdown is likely to be small.
- The Bank reviewed past judgements and recent evidence on UK consumer credit quality and has allowed for lower losses in the 2025 Bank Capital Stress Test than in past exercises.[22] The removal of past judgements is estimated to reduce the five-year impairment rate on UK unsecured personal credit portfolios in the 2025 Bank Capital Stress Test by 4.6 percentage points.

> **The FPC judges that changes to the stress-testing framework set out in this box are consistent with an unchanged risk tolerance for the resilience of the UK banking system and have avoided an unwarranted increase in capital requirements.**

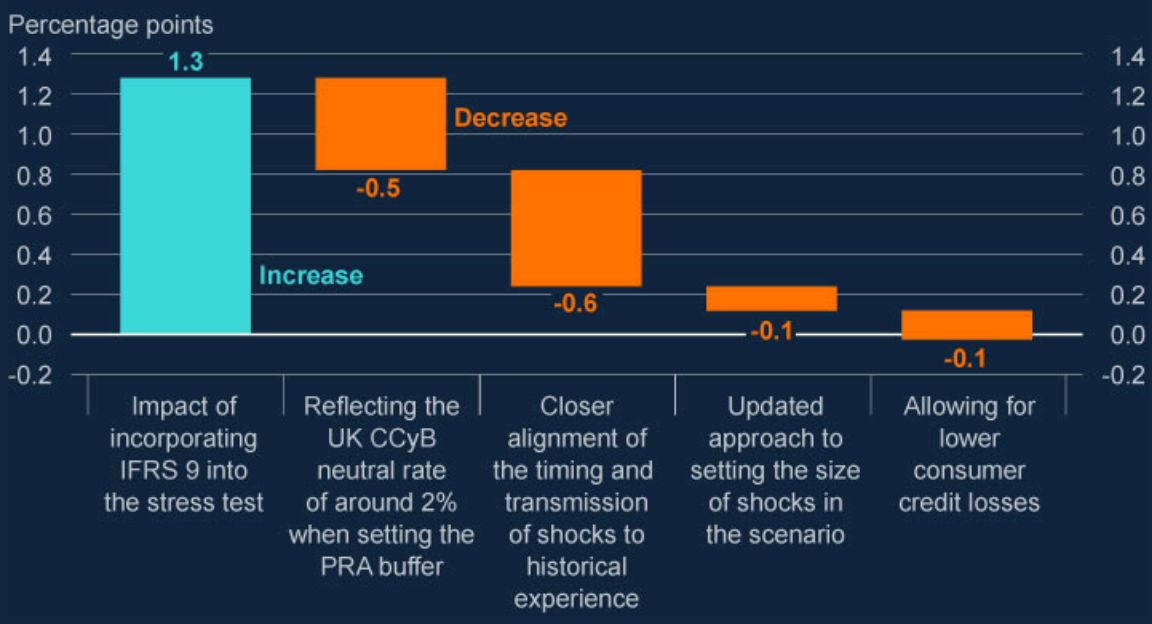
The 2025 Bank Capital Stress Test has been used to assess the net impact of IFRS 9 and changes made to the stress-testing framework. Chart A shows that the net impact of IFRS 9 and changes made to the stress test are broadly neutral on the aggregate level of capital required to absorb the impact of the stress scenario.

While the impact of changes made to the stress-testing framework will differ by bank, the Bank estimates that the net impact of incorporating IFRS 9 and the changes set out in this box into the 2025 Bank Capital Stress Test has not implied any increase in capital buffers required for any individual bank. For some banks, this is because other capital buffers, such as the CCyB and CCoB, would be sufficient to absorb the losses in the scenario.

On the basis of the Bank's assessment, the FPC judges that the net impact of changes to the stress-testing framework and IFRS 9 have avoided an unwarranted increase in capital requirements.

Chart A: The impact of IFRS 9 and changes made to the stress test are broadly neutral on the level of capital needed to absorb losses in the stress scenario

Aggregated level of capital needed to absorb losses in the stress scenario, percentage points (a)



Sources: Bank of England analysis and calculations.

(a) For the purpose of the Bank's assessment, the capital impact of IFRS 9 is estimated using the CRR 'Quick Fix', assuming 100% relief for relevant provisions. This does not affect the final capital ratio results of the stress test, as transitional capital relief has now expired.

> **The Bank intends to maintain these changes for future stress tests and expects to return to assessing resilience against the benchmark of minimum capital requirements and systemic risk buffers.**

As well as avoiding an unwarranted increase in capital requirements, the changes implemented in this year's test have had a number of other benefits. The removal of complex transitional arrangements and adjustments have made the test simpler and aligned with the accounting standard that would apply in an actual stress. The changes have made the stress test more consistent with historical advanced economy stresses in terms of the size and timing of the shocks. They also reflect the increase in usable buffers that came with the change in the neutral rate of the UK CCyB in 2019. As such, the FPC intends to maintain these changes for future stress tests.

The Bank previously set out its intention to use the 2025 Bank Capital Stress Test to assess the impact of the framework changes and IFRS 9 to inform the appropriate benchmark against which to assess banks in future stress tests. Given this intention, and as indicated in

March, bank-specific low points in the scenario have been published alongside minimum requirements in Annex 2. All banks also remain above the sum of their minimum requirements and systemic risk buffers throughout the stress scenario.

In line with international standards, and consistent with the framework set in 2018 by the FPC, systemic banks should be expected to withstand a stress that is more severe than non-systemic banks, which is reflected in their systemic risk buffers.[23] As such, in future stress tests the Bank expects to return to assessing the resilience of individual firms against the sum of minimum capital requirements and systemic risk buffers. Systemic risk buffers are, like all other capital buffers, useable to absorb losses in a real stress.

> **The changes to the stress test support the FPC's and PRA's respective primary and secondary statutory objectives.**

These changes to the test ensure that the Bank Capital Stress Test will allow an assessment of the resilience of the UK banking system to a severe but plausible scenario, consistent with the FPC's primary financial stability objective and the PRA's primary objective for safety and soundness.[24]

Using the stress test to ensure banks can absorb severe but plausible shocks and continue to lend to the UK economy, while taking action to avoid an unwarranted increase in capital requirements, supports the FPC's secondary objective and the PRA's secondary growth and competitiveness objective.

Box F: Lending to private market funds in the 2025 Bank Capital Stress Test

Private markets have grown significantly in the UK over the last two decades, and are an important source of funding for the corporate sector, as set out in Section 6. Private markets encompass different types of finance, including private equity and private credit, and covering infrastructure, real assets, real estate and venture capital.

This box outlines the analysis undertaken as part of the 2025 Bank Capital Stress Test to understand better UK banks' lending exposures to private market funds, and further work the Bank intends to do on this topic.

UK banks provide lending facilities to support private market fund activities.

Banks interact with private markets in a variety of ways, as set out in the July FSR. Within that, they can play an important role in providing loans and direct financing lines to private equity and private credit funds, who in turn invest in and lend to the corporate sector.

The FPC has previously judged that vulnerabilities in private markets – especially those related to interconnectedness, concentration, opacity around valuation and high leverage – could create risks to financial stability.

In the 2025 Bank Capital Stress Test, banks were asked to submit additional information on their banking book exposures to private market funds.

As in previous stress tests, the 2025 Bank Capital Stress Test captures how the stress would impact banking and trading books. While this has always included private market exposures, in previous stress tests it was not possible to identify separately these exposures within the credit portfolios of banks' submitted results. The additional information gathered this year focused on financing activities for funds managed by private equity or alternative investment managers. It did not include requests for additional information on banks' wider trading book exposures to private markets or exposures to other non-bank financial institutions.

As context, the major UK banks are in the process of improving their capabilities to identify and monitor risks from private markets. For example, the PRA conducted a **Thematic review of private equity related financing activities** and communicated the findings in a letter to banks' Chief Risk Officers. This stated that a number of banks were unable to uniquely identify and systematically measure their combined credit and counterparty exposures linked to the private equity sector within their overall risk data.

UK banks are estimated to have £173 billion of banking book exposures to private market funds and corporates backed by financial sponsors, including private equity funds.

Of that, the Bank estimates that UK banks have £136 billion of direct banking book exposures to private market funds. This value represents the Bank's best estimate of the size of committed limits that funds might draw on in a stress, based on the information available.[25] The exact exposure in a stress will be based on the drawn amount during the scenario. These numbers will likely evolve over time given work by participating banks to improve the quality of data collection on these exposures.

Most of these exposures are to investor-recourse facilities (£95 billion), commonly known as subscription credit lines or capital call facilities. These are lending facilities to private market funds backed by the contractual commitments of investors to provide capital to the fund, rather than the underlying assets of a fund. From a fund management perspective, these facilities provide operational flexibility, allowing fund managers to bridge the timing between investment deployment and capital calls.

The rest of the direct exposures to private market funds are asset-backed facilities (£41 billion), such as net asset value (NAV) financing. These are typically secured against a defined pool of portfolio assets, with borrowing capacity linked to their appraised value. If asset values fall below agreed thresholds, funds may need to post additional collateral or repay part of the loan to maintain compliance with covenants of the loan agreement.

In addition, banks reported committed limits of £37 billion to UK corporates which are majority-owned by financial sponsors, including private equity funds. In the stress test, these are assessed as part of banks' leveraged lending portfolios.[26] This lending tends to be riskier than other types of lending to businesses due to high levels of debt on the underlying corporates’ balance sheets.

Together, UK banks are estimated to have £173 billion of banking book exposures to private market funds and to highly leveraged corporates backed by financial sponsors. As noted above, this value represents the Bank's best estimate of the size of committed limits that might be drawn on in a stress. This is equivalent to 8% of UK banks’ total committed limits across their wholesale portfolios, or 67% of aggregate CET1%. The composition of banks’ exposures to these portfolios is set out in Table 1.

Table 1: The Bank estimates that UK banks have £173 billion of banking book exposures to private market funds and corporates backed by financial sponsors, including private equity funds.

UK banks' committed limits to private market funds and corporates backed by financial sponsors (a) (b)

Item	Committed limits (£ billions)
Lending to private market funds	136
of which: investor-recourse facilities (eg subscription financing)	95
of which: asset-backed facilities (eg NAV financing)	41
Lending to corporates who are majority owned by financial sponsors	37
Memo: Total wholesale lending	2,212

Sources: Participating banks' STDF data submissions and Bank analysis and calculations.

(a) Figures represent the Bank's best estimate of committed limits where available, or allocated business limits where committed limits were not disclosed.
(b) Financial sponsors are investment firms that undertake strategic private equity investments in or leveraged buyouts of companies with the intention of profitably exiting those investments on a medium-term basis.

Loss rates on private market fund financing lines have historically been low…

Banks have explained historically low loss rates on private market fund financing lines to be supported by capital commitments from large institutional investors and diverse asset pools with low loan to value ratios. Investors typically include sovereign wealth funds, insurance companies and pension schemes. Many of these funds are closed-ended funds, locking in investment capital during the stress until asset prices recover towards the end of the scenario.

…but many of these exposures are arguably yet to be tested in a real-world stress.

While resilient to date, private markets have grown rapidly since the global financial crisis and have not been tested through a broad-based macroeconomic stress at their current size. The structure of these markets has also evolved, with a wider set of asset managers and private credit funds making greater use of financing from banks, in addition to providing more direct lending to the corporate sector.

This makes it difficult to assess the impacts of a stress on banks and the wider financial system. The data provided by banks this year has improved the level of insight into the interconnections between banks and private finance. However, this remains a challenging area, where data remains limited on the underlying investors and assets on which bank lending to private market funds is secured.

The Bank continues to monitor risks to banks from their private market exposures.

As private market financing continues to expand and becomes more interconnected with bank balance sheets, continued monitoring is warranted to understand better the interplay between leverage, underlying collateral and asset valuations and any risks to investment capital in these markets. In particular, it will be important to understand how private market participants might respond in a stress, and whether there is potential to amplify any shocks.

The Bank will explore risks from private markets further as part of future exercises, including the upcoming system-wide exploratory scenario (Section 6).

6: The resilience of market-based finance

Monitoring and improving the resilience of market-based finance (MBF) is crucial to ensuring that the financial system can absorb shocks, rather than amplify them. This protects overall economic and financial stability and allows MBF to continue providing vital services to households and businesses.

Market-based finance is an interconnected system of markets, market infrastructure such as central counterparties (CCPs), and non-bank financial institutions (NBFIs) such as insurers, hedge funds and private finance firms. MBF has grown significantly in importance; with NBFIs now accounting for around half of global and UK financial sector assets.

Recent events – such as the March 2020 dash for cash and the 2022 liability-driven investment (LDI) episode – have highlighted vulnerabilities in the system of MBF and the risks these can pose to UK financial stability. Downside risks to the economic outlook and a potential broader market correction could interact with these vulnerabilities. The interconnected nature of MBF means it can amplify shocks, including through large leveraged hedge fund positions in sovereign debt markets.

Enhancing the Bank's understanding of risks from MBF, and the behaviours of NBFIs under stress, was a key motivation behind the Bank's **first system-wide exploratory scenario** (SWES). The Bank will undertake a SWES exercise focused on the private markets ecosystem (Section 6.3).

6.1: Developments in the resilience of the gilt and gilt repo markets

The UK gilt and gilt repo markets are critical to the smooth functioning of the UK financial system, including MBF.

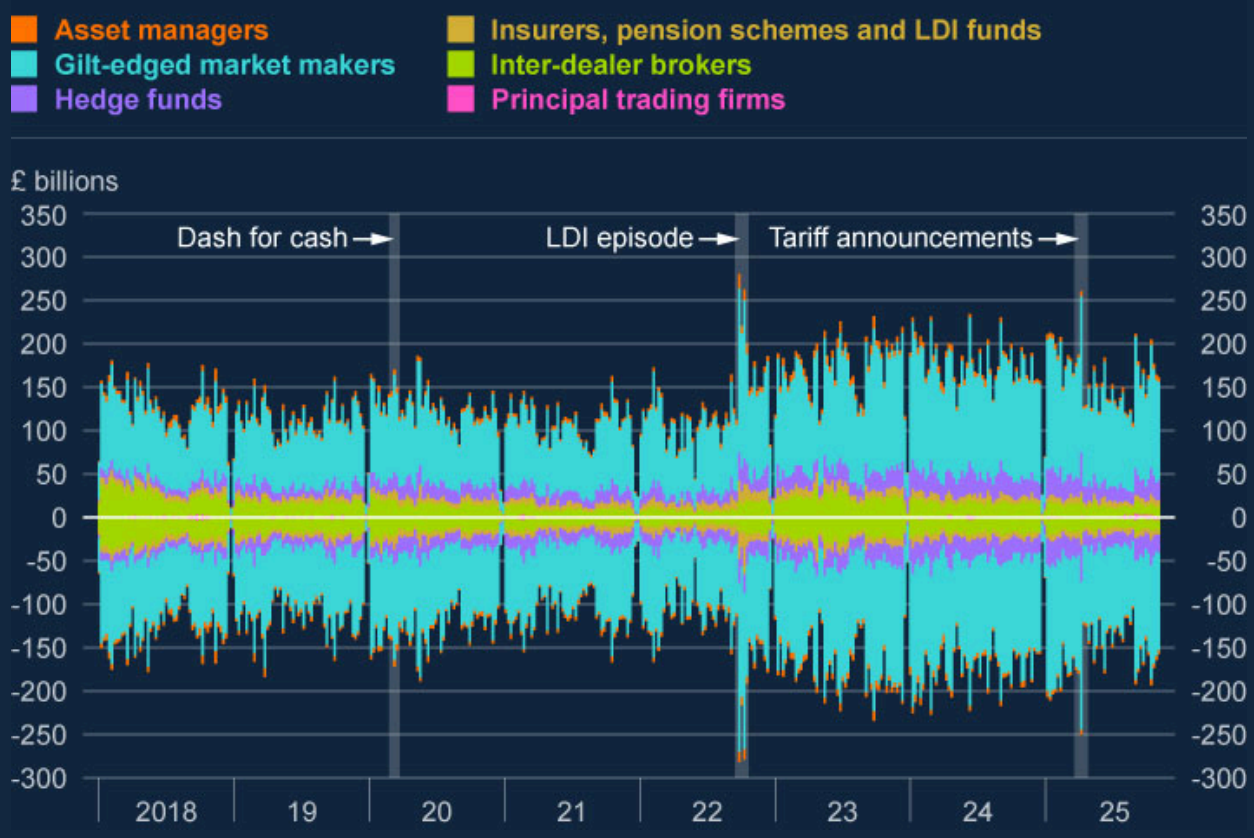
Given their role in financing government activity and as a benchmark for the pricing of other financial instruments such as corporate bonds, government bond markets facilitate the provision of vital services, investment, and sustainable economic growth. In turn, government bond repo markets are critical to the resilience of government bond markets, and therefore financial stability. Repo markets facilitate the flow of cash and gilts across the financial system and are a source of funding for market participants' leveraged strategies. NBFIs play an important role in gilt and gilt repo markets.

UK gilt and gilt repo markets have continued to function in an orderly way in 2025.

Gilt trading volumes and bid-offer spreads have remained within historical ranges since the July FSR, and well below the peaks seen during the episode of volatility in April. The spread between gilt repo rates and Bank Rate has consistently been around its recent average, with the exception of expected periods of elevated repo rates such as period end, or following large repayments of the Term Funding scheme with additional incentives for Small and Medium-sized enterprises (TFSME). Usage of the Bank's short-term and long-term repo facilities has also continued to grow as designed. The usage of these facilities was discussed in a recent **speech by Vicky Saporta**.

Chart 6.1: The gilt market has continued to function in an orderly way

Weekly gilt volume across sectors, £ billions



Sources: Financial Conduct Authority MiFID II data.

Vulnerabilities in MBF previously identified by the FPC persist. Leveraged borrowing by hedge funds in gilt repo markets remains elevated.

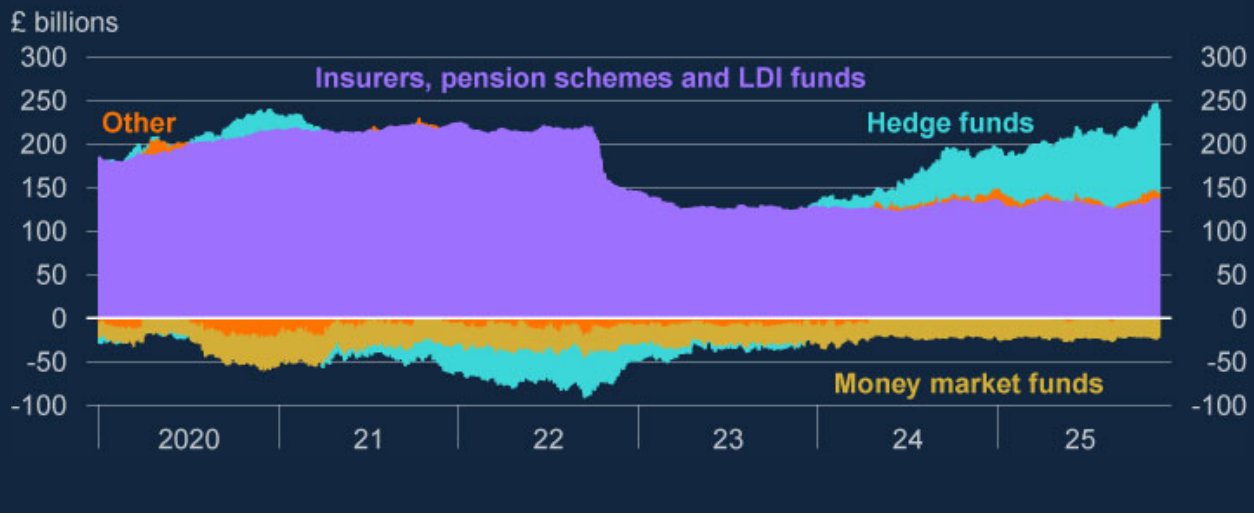
As noted in the **July 2025 Financial Stability Report**, leveraged market participants such as hedge funds, have an increasingly important role in core UK markets such as the gilt market – including cash, repo, and related derivative markets. In contrast, firms such as insurers and pension funds, who had the highest demand for gilts historically, especially at longer maturities, have become less active as higher nominal yields improve their funding ratios, and an ageing population may encourage funds to shift toward shorter-term assets to ensure liquidity for paying current benefits.

Leveraged market participants can often serve a useful function by warehousing risk and intermediating between different types of market participants, thereby improving market liquidity and price discovery. These firms also carry out forms of arbitrage between different related assets (eg between gilts and gilt futures), removing relative pricing discrepancies.

Hedge fund net gilt repo borrowing has continued to increase since the July FSR, reaching close to £100 billion in November, the highest since data collection began in 2017 (Chart 6.2).

Chart 6.2: Hedge fund net gilt repo borrowing is substantially higher than a few years ago

Net repo positioning across non-bank sectors (a)



Sources: Sterling money market data (SMMD) and Bank calculations.

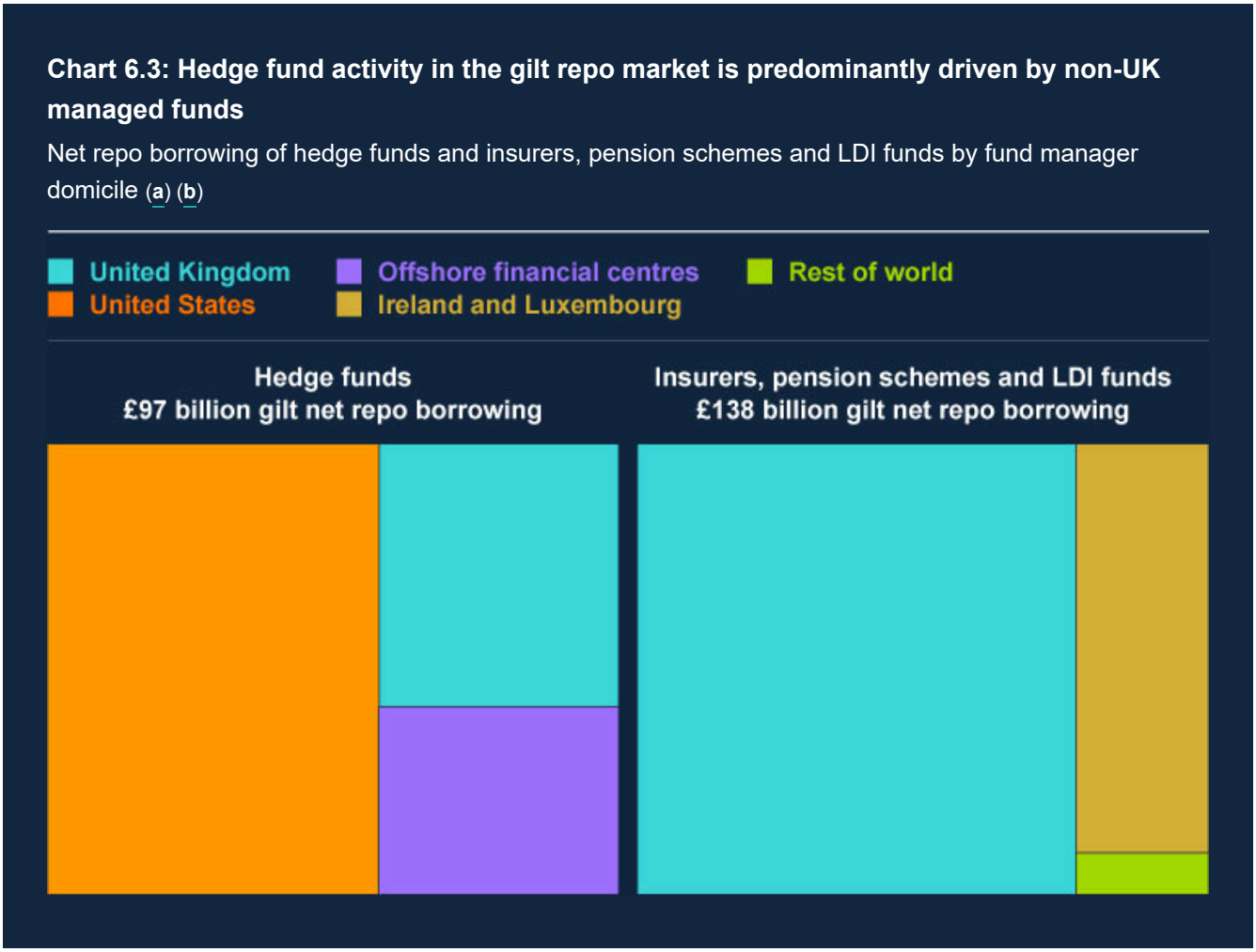
(a) Latest data as of 24 November 2025. SMMD data and the sector classification are reviewed on an ongoing basis in order to continuously improve the quality and coverage of the data set.

Net borrowing in gilt repo markets by hedge funds is concentrated and heavily driven by international firms.

Hedge fund leveraged positions in the gilt repo market are predominantly driven by entities that are managed outside the UK, with hedge funds managed by US managers accounting for around 60% of hedge funds' total net gilt repo borrowing (Chart 6.3).[27] More long-standing participants in the gilt market such as pension and LDI funds are mostly managed from within the UK, even though a large proportion of pooled LDI funds are domiciled in Ireland and Luxembourg. The growing role of multinational NBFIs is also evident in other sovereign debt markets (Section 2). This increases cross-border spillover risk, as well as opacity for regulators' domestic risk assessments, highlighting the importance of international co-operation and data sharing.

Chart 6.3: Hedge fund activity in the gilt repo market is predominantly driven by non-UK managed funds

Net repo borrowing of hedge funds and insurers, pension schemes and LDI funds by fund manager domicile (a) (b)



Sources: Global Legal Entity Identifier Foundation (GLEIF) Level 1 and Level 2 data, SMMD and Bank calculations.

(a) For insurers and pension schemes, this chart shows the domicile as reported under SMMD. For hedge funds and LDI funds the chart shows the domicile of the fund manager, not of the fund itself. Where the fund and not the fund manager was reported, Bank staff used GLEIF level 2 data to identify the fund manager. The fund manager might still have an ultimate parent in a different jurisdiction. Where no GLEIF level 2 data was available, Bank staff used the reported domicile. This may lead to an overestimation of the share of hedge funds managed by fund managers in offshore financial centres and may underestimate the share of hedge funds managed by US hedge fund managers.
(b) Offshore financial centres include the Cayman Islands, Virgin Islands and Jersey.

> **Data suggest that the increase in activity and leveraged borrowing by hedge funds in the gilt repo market is related, at least in part, to the popularity of the cash-futures basis trade among these firms (Chart 6.4).**

The cash-futures basis trade is one example of a leveraged strategy set out in the **July 2025 Financial Stability Report**. Data suggest this trade has been a driver of growth in gilt repo borrowing by hedge funds. At present, the cash-futures basis trade is one where hedge funds purchase gilts (financed via repo, typically provided by banks) and sell gilt futures contracts, taking advantage of the discrepancy of the forward price of the gilt and the price of the futures contract into which it can be delivered, and therefore benefiting from the small price differential. As the return on this trade is small, it is often done at high levels of leverage to boost overall returns. The repo leg of this trade can often be done at a zero haircut, sometimes because dealers are able to

net with margins of the offsetting futures, or other positions, in the same client portfolio.[28] Hedge fund gilt repo borrowing is often done at short maturities, often overnight, and so requires regular refinancing to maintain positions.

UK EMIR trade repository data indicates that the cash-futures basis trade is heavily populated by hedge funds, with data showing funds are increasingly short in gilt futures, and therefore likely exposed to the cash-futures basis. This activity is heavily concentrated: a small number of hedge funds account for more than 90% of all net gilt repo borrowing by hedge funds.

Chart 6.4: Data suggest that hedge fund net gilt repo borrowing is related, at least in part, to the popularity of the cash-futures basis trade

Growth in hedge fund net gilt repo borrowing and gilt futures open interest since January 2024 (a)

Sources: ICE Futures Europe, SMMD and Bank calculations.

(a) Spikes in gilt futures open interest refer to contract roll periods – eg as seen in most recent data.

Relatively high use of leverage by a small number of firms taking crowded positions increases vulnerabilities and the risk of a disorderly unwind of positions and a jump to illiquidity in core UK markets.

These vulnerabilities, in the context of compressed risk premia, in a highly uncertain global environment, increase the risk of sharp moves (Section 2). The small number of funds running crowded and heavily leveraged trades in the gilt repo market increases the potential risk of sharp moves as funds could need simultaneously to deleverage in response to a shock. The **July 2025 Financial Stability Report** outlined four common triggers that could lead to forced or widespread deleveraging of leveraged trades.[29]

Forced or widespread deleveraging would have the result of amplifying initial moves and potentially triggering a feedback loop of further forced selling, especially if funding conditions tightened to the extent that refinancing became unavailable or prohibitively expensive. Banks' potential unwillingness to roll repo financing due to counterparty concerns or balance sheet constraints, was a key finding of last year's SWES. This reinforces the need for market participants to risk-manage their positions to take account of potential shocks, including correlation shifts outside historical norms.

The opacity of parts of the gilt repo market can impact effective risk management of leveraged strategies. Authorities can lack visibility of some trades not involving a UK domiciled clearing member. In addition, prime brokers have limited visibility of their clients' portfolios across counterparties and therefore can be unaware of the total leveraged exposure of their counterparties.

> **The FPC welcomes work by the Bank to evaluate potential reforms to enhance the resilience of the gilt repo market.**

In September, the Bank, in close consultation with the FCA, and with input from HM Treasury and the UK Debt Management Office, published a **discussion paper** evaluating the effectiveness and impact of a range of potential reforms to enhance the resilience of the gilt repo market. These include greater central clearing of gilt repo and minimum margin requirements on non-centrally cleared gilt repo transactions. Any structural reforms identified through this work will take time to implement, which underscores the importance of market participants ensuring their own preparedness for shocks.

After reviewing responses to the discussion paper, the Bank will publish a feedback statement and continue to engage with industry on any potential measures. A **recent speech by Lee Foulger** outlined key insights from industry engagement on this discussion paper.

6.2: US credit defaults and risky credit markets

> **Two recent high-profile corporate defaults in the US have intensified focus on potential weaknesses in risky credit markets previously flagged by the FPC.**

These include high leverage, weak underwriting standards, opacity, complex structures, and the degree of reliance on credit rating agencies, and illustrate how corporate defaults could impact bank resilience and credit markets simultaneously.

Losses in one risky credit market not only directly generate losses for banks and institutional investors, but also have the potential to cause spillovers to interconnected markets and other forms of risky credit. This could reduce investor confidence, trigger a widening in spreads, and tighten financing conditions for businesses.

Markets have broadly seen the defaults of First Brands and Tricolor as driven by company-specific challenges, including alleged fraud, with no material repricing in credit markets (Section 2). However, it is prudent for market participants to assess fully what lessons can be learned from

these defaults, including what they could reveal about wider risks to individual firms and to global financial stability arising from the private markets and risky credit ecosystems – despite the fact that these two companies only used limited private financing.

Both First Brands and Tricolor had complex and opaque funding arrangements and were highly leveraged, including through use of off-balance sheet debt. First Brands funded itself via syndicated term loans, often purchased by collateralised loan obligations (CLOs), and use of asset-backed lending and factoring. Tricolor provided sub-prime auto loans to consumers which it then securitised and sold as asset-backed securities (ABS), using warehousing facilities from lenders as a 'bridge' until it had enough loans to securitise. Lenders were not fully aware of the level of off balance sheet debt, nor the overall levels of leverage operated by the companies, suggesting potential opacity in financial disclosures.

The opacity and complex structures may have been a contributing factor that allowed significant alleged fraud to go undetected for a period. There have been reports in both cases, as well as some other recently publicly disclosed losses, that the collateral against which lending was secured was misrepresented or even fraudulent.[30] These episodes reinforce the need for lenders to maintain high-quality underwriting standards and collateral verification when lending to opaque and complex structures. The number and variety of lenders affected, and the inability to detect alleged fraud or off balance sheet exposures, highlight potential weaknesses in underwriting standards as previously highlighted by the FPC during the low rates era. Weaknesses previously highlighted include the increasing share of leveraged loan deals with weaker covenants, a rise in the use of earnings add-backs to reduce headline leverage multiples, and looser documentation standards.

This episode demonstrated the complexity and interconnectedness of the broader risky credit ecosystem, with a significant range of banks, insurers and NBFIs facing losses and uncertainty over where risk was held. Interconnections across financial markets may heighten systemic vulnerabilities, particularly under stress conditions, by reinforcing correlations and amplifying shocks. A shock to risky corporates could be amplified by these interconnections, with losses and the impact on risk appetite potentially spilling across several markets and sectors.

> **The defaults of First Brands and Tricolor highlighted potential weaknesses that, if widespread, could lead to systemic issues.**

While the impact of these specific defaults has been limited, a diverse range of financial market participants were exposed. Such diversity can help absorb risks, but opacity around the extent of exposures, and their possible interconnections, can also create uncertainty about how widely shocks in credit markets can propagate. It is important that market participants have a clear understanding of their exposures, including in stress scenarios where correlations and losses can shift outside historical norms. Market participants should also ensure that underwriting standards are robust and that they do not over-rely on credit ratings as a substitute to carrying out appropriate due diligence.

If the vulnerabilities highlighted by these defaults were widespread, then similar defaults could follow and potentially lead to systemic issues, especially if broader economic conditions deteriorate. In this case, opacity and the lack of knowledge about where risk is held given interconnections, and concerns about ratings and valuations, could increase uncertainty over counterparty risk in funding markets. In extreme, risks crystallising in the US could spill over to UK financial institutions and markets through contagion and direct exposures, tightening the availability of credit to the UK financial system, households and businesses. This could be more pronounced than in some other markets given that 70% of private markets financing comes from outside the UK.

> **These defaults also demonstrated the risks associated with reliance on credit rating agencies (CRAs). First Brands and Tricolor's ABS loans maintained a stable credit rating until relatively close to default. Relatedly, there is some evidence that the use of smaller CRAs has been growing in parts of the market.**

Credit ratings are a well-established and widely used way to assess the credit risk of corporates, financial institutions, sovereigns and securitisations. The defaults of First Brands and Tricolor highlighted the risks of reliance on CRAs. The rating of First Brands – even if speculative grade – was stable until relatively close to default. In addition, some securitised tranches of sub-prime auto loans made by Tricolor maintained a high rating until close to failure.

CRAs can play an important role in credit markets by providing independent assessments of credit risk based on transparent, published methodologies. This includes the rating of debt portfolios and structured credit vehicles such as CLOs and ABSs. **Recent research by the Bank for International Settlements** highlights the challenges in accurately assessing the risk of ABSs.

Unlike public markets, such as corporate bonds, where liquid secondary markets can be the source of an up-to-date independent valuation, as well as providing other signals on the outlook or risks of an investment, private assets rely on a mix of internal models and benchmarking from public markets. This means that valuations and ratings in private markets can be less transparent and less standardised (**read findings from the FCA's review of private market valuation practices**).

There has been increased use of confidential rating assessments in recent years, both in the form of Private Letter Ratings (PLRs) and through less comprehensive assessments via credit opinions (or estimates) – an informal, point-in-time assessment of credit worthiness. In both cases the rating is confidential, increasing opacity. Data on the use of these private assessments is limited but **BIS research** has highlighted the growing use of PLRs in parts of the US insurance market (23% of PE-linked insurers and 8% of non PE-linked investments used PLRs at end-2024). One example of the growing use of credit estimates is S&P, who have reported the volume of credit estimates they provide has more than doubled since 2021, with growth especially among CLO managers.

There has been an increase in the number of small CRAs in recent years,[31] and some market speculation that competitive pressures could provide incentives for some CRAs to provide ratings that are designed to win custom. Smaller CRAs can in some instances provide ratings more quickly

and for a lower cost than larger CRAs which can be beneficial, but only if the quality and rigour of the rating is not compromised.

Given the importance of ratings provided by CRAs in the financial system, a loss of confidence in the accuracy of credit ratings could undermine confidence in financial institutions and markets where CRAs play a prominent role, and ultimately impact the supply of finance to the real economy. This underscores the risks of firms over-relying on credit ratings providers as a substitute to carrying out appropriate due diligence.

6.3: Private markets system-wide exploratory scenario

> **Private markets have grown significantly in the UK and are an important source of funding for corporates.**

Over the past two decades, the amount of capital deployed in private markets has grown substantially; estimates put the total assets under management employed in private markets strategies at over $15 trillion globally.[32] Private markets encompass various forms of financing, including private equity, venture capital, and private credit, spanning infrastructure, real estate, other real assets, and corporate lending.

In the UK, private markets have become an increasingly important source of finance for corporates. UK corporates that are backed by private equity investors account for up to 15% of total UK corporate debt and 10% of private sector employment (over 2 million employees).

The growth of private markets is beneficial for businesses and the wider economy. It has broadened the types of capital available to the real economy, bringing benefits from greater competition and diversification. A variety of providers of capital, with a wider range of risk appetites, has generated greater availability of finance for businesses, and greater capacity to take a longer-term perspective or to support challenging business plans such as turnarounds. Some academic literature finds evidence that private equity ownership enhances portfolio firms' operational efficiency, driving innovation, investment, and financial performance.[33]

> **While resilient to date, the private market ecosystem has not been tested through a broad-based macroeconomic stress at its current size.**

While the growth of private markets has provided benefits for UK corporates, they are untested in a macroeconomic downturn at their current size. The sector is currently facing challenges from high interest rates and a weaker and more uncertain growth outlook. These factors are making it challenging for funds to sell portfolio companies and distribute returns to investors. This has led to funds increasingly using other strategies to provide returns to investors, such as continuation vehicles that transfer ownership of selected portfolio companies to a new fund.

> **In order to enhance understanding of the broader risks and dynamics of private markets, the Bank will undertake its next SWES exercise, focused on the resilience of the private markets ecosystem.**

While the FPC and other authorities currently monitor private markets, data gaps and the need to look at this system of finance in its entirety make it hard to assess the potential for systemic risks to occur in these markets. This is a challenge also faced by other financial stability authorities and regulators internationally.

In light of this, the Bank will undertake a SWES exercise focused on the private markets ecosystem, which will aim to:

- Explore risks and dynamics associated with private market finance through understanding the actions taken by banks and NBFIs active in private markets in response to a shock, and how these actions may interact at a system level.
- Understand whether these interactions can amplify stress across the financial system and pose risks to UK financial stability and the provision of finance to the UK real economy.

The SWES will improve the Bank's understanding of the behaviours of banks and NBFIs active in the private markets ecosystem in response to a downturn, and whether those behaviours will amplify stress across the financial system and pose risks to UK financial stability.

The exercise is not a test of the resilience of the individual firms that will participate in the exercise. Its focus is system-wide in exploring the resilience of the provision of private market and related public market finance to the UK corporate sector.

The Bank will publish further information on the SWES soon.

6.4: Improving the resilience of market-based finance

> **Market surveillance plays a key role in identifying financial stability risks, including those from leveraged participants.**

The Bank monitors leverage, interconnectedness and concentration in core markets using transaction-level data, market intelligence, and system-wide exercises like the SWES. Data published in this FSR (eg net gilt repo borrowing across sectors) is intended to contribute to market participants' understanding of their exposures relative to the aggregate market and help inform their risk management and preparedness for future shocks. The FPC intends to expand the data it publishes in this area.

> **The Bank is investing in its ability to monitor and assess systemic risks in UK financial markets, including gilt and sterling corporate bond markets.**

Building on the **first SWES** exercise, Bank staff are developing a desktop-based system-wide stress testing capability, as well as other related tools. This will allow for periodic updates to the SWES findings as the financial system and risk-taking behaviours evolve, more quickly and at lower cost than a full SWES exercise.

The **July 2025 Financial Stability Report** described a tool developed by Bank staff to estimate the losses incurred by LDI funds, and the size of any resulting capital calls to investors, under different interest rate scenarios. Other key areas of work include: estimating the impact of margin calls on the liquidity buffers of market participants that use derivatives and repo, and inferring the actions they then take to restore those buffers; understanding how investors in open-ended funds respond to price shocks; and modelling how hedge funds behave in periods of heightened volatility. Bank staff have discussed their plans with participants in the first SWES exercise. Alongside continued engagement with financial market participants, this will allow the FPC to improve its assessment of risks by taking a system-wide perspective.

> **The FPC seeks to strengthen the resilience of MBF to mitigate risks to UK financial stability. Where effective and practical, it works to address vulnerabilities domestically while recognising that for many risks, mitigations require international co-ordination.**

Given the interconnected nature of MBF, reforms to improve resilience are most effective when co-ordinated internationally. Table 6.A provides a summary of progress against building resilience in MBF domestically and internationally.

Table 6.A: Overview of progress on building resilience against key vulnerabilities in MBF domestically and internationally (a)

Vulnerability	Financial stability implications	Policy recommendations and next steps
Liquidity mismatch in money market funds (MMFs)	MMFs are used by UK corporates, investment funds, and other NBFIs as a way of managing cash balances. Investors hold around £300 billion in sterling-denominated MMFs. Liquidity mismatch between the redemption terms and the liquidity of some of their assets makes MMFs vulnerable to sharp redemptions from investors in stress and so creates the risk of both runs and contagion across the sector. This could amplify shocks, impact financial stability if investors cannot access cash, and lead to tighter financial conditions for the economy.	The Financial Conduct Authority (FCA) launched a consultation paper on enhancing MMF resilience measures, in December 2023. This work is part of broader international efforts to address vulnerabilities and increase the resilience of MMFs, in line with the principles set out by the Financial Stability Board (FSB). In February 2024, the FSB published a **Thematic review on money market fund reforms** in national authorities, taking stock of measures adopted or planed by FSB members. The report highlights uneven progress on the implementation and recommends further action in particular regarding increasing liquidity requirements. Follow-up work is planned by the FSB in 2026 to assess the effectiveness of those measures. **The FSB has also published a report** (May 2024) enhancing the resilience of commercial paper and commercial deposit markets.
Liquidity mismatch in open-ended funds (OEFs)	Globally, the assets under management of OEFs primarily investing in UK equities, sterling government bonds, sterling corporate bonds, and UK property totalled around £234 billion, £51 billion, £85 billion, and £13 billion respectively as of October 2025. Some OEFs offer daily redemptions while holding less liquid assets. This means in stress, there is an incentive for investors to redeem ahead of others. Funds may struggle to meet **redemption demands without rapid sales of assets, which could lead to contagion across markets.**	In December 2023, the FSB published a set of revised policy recommendations to address structural vulnerabilities from liquidity mismatch in OEFs, complemented by new International Organization of Securities Commissions (IOSCO) guidance on anti-dilution liquidity management tools. The FSB and IOSCO will undertake a stocktake, to be completed in 2026, of the measures that have been adopted and planned, with a further effectiveness review by 2028 to see whether financial stability risks have been sufficiently addressed.

Non-bank leverage	Leverage creates counterparty risks and can lead to sudden spikes in demand for liquidity – either to support the financing of leveraged positions, or as deleveraging leads to forced sales, which in turn could amplify shocks and lead to market dysfunction and a potential tightening in financial conditions for households and businesses. The notional amount of non-bank investors' over-the-counter derivatives in 2022 has been estimated at almost $90 trillion. Global NBFI financial debt in 2022 has been estimated at approximately $48 trillion, or 50% of global GDP.	The **FSB has published policy recommendations** to enhance authorities' ability to identify, monitor and mitigate the risks associated with non-bank leverage in June 2025. The policy recommendations propose a robust set of metrics and policy tools (eg activity and entity-based measures) to monitor leverage as well as contain the financial stability risk of leverage. The FPC supports the implementation of these recommendations. **The FCA is reviewing its data collections to ensure its reporting regimes support the monitoring and identification of risks, while remaining proportionate and removing unnecessary reporting. The Bank launched a discussion paper on potential reforms to enhance gilt repo market resilience. The call for responses has now closed and the Bank will respond to feedback in due course.**
Liquidity demands from margin calls in stress	Margin can increase rapidly in stress to match the increase in expected potential losses and risks. Increases in margin that are unpredictable or unexpectedly large can cause liquidity strains on market participants and the financial system. For example, during the March 2020 dash for cash, initial margin requirements at UK CCPs increased by around 31% to £58 billion, and average daily variation margin calls were five times higher than in January and February 2020.	**The FSB published its final set of policy recommendations to enhance liquidity preparedness of market participants in December 2024. These policy recommendations aim to enhance the liquidity preparedness of NBFIs for margin and collateral calls in centrally and non-centrally cleared derivatives and securities markets. Recommendations cover liquidity risk management and governance, stress testing and scenario design, and collateral management practices.** The Bank has continued to co-chair the Basel Committee on Banking Supervision, the Bank for International Settlements' Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions Margin Group responsible for work to improve the transparency and evaluate the responsiveness of initial margin practices in centrally cleared markets. The FSB published its **final set of policy recommendations** in December 2024. This work is expected to culminate in updates to international standards and guidance in 2025. The Bank will look to enhance its domestic CCPs margin framework in line with these proposals.

Capacity of markets to intermediate in stress without compromising on the resilience of dealers	Past episodes of market turbulence, such as the 2020 dash for cash and the 2022 LDI episode have shown that vulnerabilities in NBFIs can propagate liquidity stresses in the gilt market, via investor deleveraging, liquidity mismatches in funds, liquidity demands from margin calls and insufficient market participant preparedness to meet rising margins. Exacerbated by limited dealer intermediation capacity, these events have led to periods of forced selling of gilts by NBFIs and self-reinforcing price spirals, threatening UK financial stability.	The FPC had previously noted that there would be value in exploring ways to enhance market intermediation capacity in a stress, without compromising dealer resilience, including through potential changes to market structure. **The Bank recently published a discussion paper looking at enhancing the resilience of the gilt repo market. The reforms here (including greater central clearing) would enhance market intermediation capacity.** The FPC also welcomed the progress the Bank had made in developing a new lending facility, the Contingent NBFI Repo Facility (CNRF), to address severe market dysfunction in the gilt market that threatens UK financial stability arising from shocks that temporarily increase NBFIs' demand for liquidity. The CNRF opened for applications in January 2025. As a contingent facility, the CNRF will be activated at the Bank's discretion and will lend cash to participating insurance companies, pension funds and LDI funds against UK sovereign debt (gilts) for a short lending term. To support market participants, the Bank has published an updated **Market Notice (28 January 2025)** to provide details about the CNRF, including how firms can start the process of applying.

(a) New policy developments are in **bold**.

7: Structural changes in the UK financial system

This section updates on the FPC's assessment of structural changes in the UK financial system.

The financial system is constantly evolving, and new risks emerging, as technological, economic, geopolitical, and broader societal shifts change the landscape in which it operates. This evolution – and the emergence of new risks – can have material implications for the provision of financial services to households and businesses, and for the FPC's primary and secondary objectives.

The rapid pace of change under way currently presents a range of opportunities and risks. Technological innovation has the potential to improve the way in which the financial system serves households and businesses, and their resilience to financial and economic shocks, and to reshape the UK economy, boosting productivity and economic growth. But innovation can also present new risks to the stability of the financial system and its contribution to growth. Changes in the economic and geopolitical environment can further expose new vulnerabilities that reduce the resilience of the financial system. Resilience to risks from these structural changes therefore allows the financial sector to make the most of the opportunities they present.

The FPC works to identify new risks, including through horizon scanning, and builds its approach to individual risks over time (as it already has done on operational resilience, cryptoassets, stablecoins, and artificial intelligence (AI)). These opportunities and risks, and the interconnections between them, will remain an enduring focus over the FPC's policy horizon. And future FSRs will seek to communicate the FPC's views and actions on these as appropriate.

This section focuses on three areas where there have been developments in recent quarters: operational resilience; climate-related risks; and developments in unbacked cryptoasset and stablecoin markets.

7.1: Operational resilience

Heightened geopolitical tensions and continued advances in technology have underlined the critical importance of operational resilience to the provision of vital services to households and businesses. Against this backdrop of considerably heightened risk, the FPC supports further actions to be taken by firms and financial market infrastructures (FMIs) to build resilience to operational disruption.

In March 2024, the FPC set out its **macroprudential approach to operational resilience**, which highlighted the growing risks to financial stability from operational issues and the importance of system-wide resilience (in addition to the resilience of individual firms).

Since then, risks to operational resilience have continued to grow.[34] A record share of respondents to the Bank of England's **Systemic Risk Survey** cited cyberattacks (86%) and operational risks (36%) in their top five risks to the UK financial system in 2025 H2. In 2025, the

National Cyber Security Centre (NCSC) reported over 200 nationally-significant cyber incidents, up from 62 in 2023. The significance of these risks – and their potential to affect activity, revenues and valuations severely – has been highlighted by major incidents affecting national infrastructure, UK retailers and vehicle manufacturers this year.

This increase in risk reflects increased geopolitical tensions and advances in technology. Elevated geopolitical tensions have been associated with an increase in cyberattacks globally. New technologies such as AI and Distributed Ledger Technology (DLT) provide benefits to some firms, and increased automation may reduce operational risks. But they may also introduce new operational risks related to speed, explainability, insufficient controls, and outsourcing including to critical third parties. New technologies may also increase the capabilities of cyberattackers. In future, development of large-scale quantum computing could undermine the security of public key cryptography, upon which many computer systems, including financial software, are dependent. The NCSC has therefore **set out recommended timelines** to migrate to post-quantum cryptography (PQC). Preparing and planning for PQC migration now – including mapping the software and hardware needed to provide key services, and dependencies between them – will mean firms and FMIs can migrate securely and in an orderly fashion, before quantum-based cyberattacks become widespread.

Together, geopolitical and technological developments further increase the likelihood that operational incidents could affect the provision of vital services such as wholesale and retail payments, clearing and settlement, and other related activity such as custody services. If such services are disrupted, it could affect the ability of financial sector participants, households and businesses to manage risk, transact or access financing. Importantly, disruption to vital service provision could undermine confidence in the financial system, and therefore negatively affect saving, investment, and economic growth.

Therefore, the FPC supports further actions to be taken by firms and FMIs to build resilience to operational disruption, including to emerging risks from AI and quantum computing and as the risk environment continues to evolve.

> **The appropriate management of high-impact operational risks by critical firms and FMIs is essential for system-wide operational resilience. Therefore, the FPC welcomes work by microprudential regulators to continue to strengthen the regulatory framework for operational resilience.**

In line with the heightened risk environment, microprudential regulators including the Bank, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) have continued to strengthen the regulatory framework for operational resilience.

In November 2024, the Bank, PRA and FCA published **final policy and rules for Critical Third Parties** (CTPs), as well as information on how they will approach CTP oversight. The overall objective of the oversight regime for CTPs is to manage risks to the stability of, or confidence in, the UK financial system that may arise due to a failure in, or disruption to, the services that a CTP provides to regulated firms and FMIs. While no designations have been made to date, preparations

are advancing and HM Treasury officials are in the process of gathering the necessary evidence to support decision making on designation. The authorities remain committed to delivering it successfully.

Recent actions taken by the Bank and PRA are set out in **the Bank of England's supervision of financial market infrastructures Annual Report 2025** and the **PRA Annual Report 2024/25**, as well as the **Thematic findings from the 2024 Cyber Stress Test**. Since these were published, authorities have continued to engage with firms and FMIs, and published **effective practices** observed across systemic firms and financial market infrastructures, highlighting the continued evolution of their cyber response and recovery capabilities.

The FPC welcomes these actions. Given the potential severity of operational disruptions, investing in resilience to severe but plausible operational risks, including developing cyber incident response playbooks and testing responses to operational events, provides a net benefit to firms and FMIs as well as their customers. When critical firms, FMIs, third parties, and the wider financial system are resilient, the risk of threats to vital services can be reduced. Firms and FMIs will also be able to respond to and absorb shocks, limiting their transmission across the financial system and to the real economy.

In taking steps to build resilience, firms and FMIs should recognise the role they play in supporting confidence in the financial system, and how disruption to vital services could negatively affect saving, investment and economic growth. For example, FMIs are required to take account of risks to UK financial stability when identifying their important business services – as set out in a recent speech by **Sasha Mills** – as are some of the largest firms. To support this, the **Thematic findings from the 2024 Cyber Stress Test** provides tools to facilitate discussion of financial stability issues between subject matter experts from a range of disciplines, as well as illustrative examples of mitigation actions firms and FMIs can take.

> **Boards of firms and FMIs should work with authorities to use the findings of sector-wide exercises and stress tests such as SIMEX and the Cyber and Operational Resilience Stress Test to improve their understanding of actions they can take to mitigate impacts on financial stability. Given the interconnected nature of the global financial system, the FPC supports further international engagement on operational resilience.**

The resilience of individual firms and FMIs alone may not be sufficient to ensure system-wide resilience: some additional vulnerabilities exist at the level of the system. As set out in the FPC's **macroprudential approach to operational resilience**, macro vulnerabilities in the financial system arise from structural features, interconnections, concentration, common dependencies, and correlated behaviours, which can amplify operational disruptions and create systemic risks beyond those faced by individual firms or infrastructures.

The Bank continues actively to test resilience to these macro vulnerabilities and transmission channels, including through scenario analysis. For example, staff have conducted a scenario exercise exploring the impacts of a cyberattack on a hypothetical third-party technology provider in core UK markets during a period of financial stress. This demonstrated that cyberattacks have the

potential to accelerate and amplify impacts on market confidence, exacerbating risk aversion and liquidity challenges. In the scenario, cross-authority and cross-industry initiatives such as the **Authorities' Response Framework** and **Sector Response Framework**, and **guidance on disconnection/reconnection** acted as mitigants to the stress' severity and duration. This emphasises the importance of cross-industry collaboration for building financial system-level operational resilience – as recently highlighted in a speech by **Liz Oakes**.

System-wide resilience is also supported by cross-industry scenario exercises and stress tests. For example, the Cross Market Operational Resilience Group (CMORG) consists of wholesale and retail banks, FMIs, insurers, authorities and the NCSC, and enables firms to share expertise and build co-ordinated strategies to minimise the impact that incidents can have. CMORG's programme of sector-wide exercises such as **SIMEX** allows firms and authorities to prepare for operational disruption by improving collective understanding of how firm-level responses to a given scenario, when taken together, shape outcomes at the market or system level. Similarly, the FPC intends that future Cyber and Operational Resilience Stress Tests (CORSTs) continue to support firms' and FMIs' understanding of their role as systemic risk managers and the actions they can take to mitigate impacts on financial stability.

Boards of firms and FMIs should use these exercises alongside findings from their own operational resilience testing, sector exercising, and lessons from real incidents to inform their understanding of their role in the wider financial system and so their approach to operational resilience. For example, the **Thematic findings from the 2024 Cyber Stress Test** highlighted that it is important for FMIs to work with the sector to ensure their members understand the complexity and implications of disconnection and reconnection and can make informed, risk-based decisions which reflect the financial stability implications of these impacts. Boards may also use published **effective practices** to support conversations about operational resilience including whether firms or FMIs have clear plans for restoring critical data from back-ups following a cyberattack, including whether they can rebuild critical applications and core infrastructure, or how they will fail over to a separate environment. Further, because cyberdefence can be challenging and costly for smaller firms (Box A), Boards, firms and FMIs should consider the appropriate level of assurance that their material third parties – which may be smaller firms – are sufficiently resilient to operational risks.

Given the interconnected nature of the global financial system, the impact of operational incidents in one jurisdiction can quickly spill over into another. The FPC supports the UK financial authorities' continued engagement internationally through a range of multilateral and bilateral channels such as via the **Financial Stability Board** and the **G7 Cyber Expert Group**. The G7 Cyber Expert Group recently issued a **statement on artificial intelligence and cybersecurity**, encouraging jurisdictions to monitor ongoing developments, promote public-private-academic collaboration, and proactively address the emerging and evolving cybersecurity risks AI may pose. The FPC encourages further multilateral international work to build resilience to operational risks which may affect global financial stability including via globally systemically important markets.

Although it is not a substitute for building appropriate resilience, the availability of appropriate cyberinsurance may mitigate material financial impacts arising from cyber risks, including outages and ransomware attacks.

Several major incidents within the UK this year have demonstrated that cyberincidents can result in material financial as well as operational impacts, particularly where a supply chain is impacted. Although it is not a substitute for building appropriate resilience, cyberinsurance can provide vital financial risk transfer for losses arising from cyberattacks and non-malicious incidents, such as outages. This can include losses sustained due to business interruption, as well as the costs incurred from responding to and recovering from an attack or incident. The availability of appropriate cyberinsurance may act as a financial safety net during incident response and recovery. And **guidance** by the NCSC suggests that the support cyberinsurers provide to improve policyholders' operational resilience may aid businesses – in this case firms and FMIs – in responding and recovering during an incident.

Insurance coverage for cyber risks is currently low. According to **Munich Re**, less than 5% and possibly as little as 1% of cyber risks are currently insured. And only 7% of UK businesses **surveyed by the Department for Science, Innovation and Technology** (DSIT) had a specific cyber security insurance policy in 2025, although 45% reported being insured against cyber security risks in some way. This low insurance coverage can be driven by a range of factors. On the supply side, factors may include limited appetite from insurers and reinsurers given cyber is complex to model as a systemic and human-driven risk, which evolves as technology and the geopolitical risk environment change. On the demand side, factors include limited awareness of product availability, and difficulties with affordability. For example, a 2025 DSIT **report** found that for UK small and medium businesses, insurance may be unaffordable, especially for firms with limited security budgets. This relates to broader difficulties small businesses face in building operational resilience – particularly the high technology cost of building and maintaining resilience against cyberthreats (Box A).

As part of wider efforts to improve resilience to cyber risks, there is an opportunity for greater collaboration between insurers and other financial firms to increase the visibility of financial impacts arising from cyber risks and the role of insurance risk transfer. Such collaboration can enable informed decision-making around risk, including where risks are not being insured. This includes where risks may ultimately be insured by governments which often act either explicitly or implicitly as insurers of last resort.

7.2: Developments in unbacked cryptoasset and stablecoin markets

The FPC recognises that DLT and tokenisation have the potential to change how the financial system operates. DLT enables the creation of common shared ledgers which can be updated near-simultaneously across all parties in a financial transaction, while tokenisation enables financial assets to be digitally represented ('tokenised') on such shared ledgers and settled near-

instantaneously. A range of digital assets utilise this technology, including but not limited to, unbacked crypto, stablecoins, and tokenised deposits and other tokenised assets backed by traditional instruments such as bonds and equities.

These technologies and their associated digital assets could reduce frictions and inefficiencies through 24/7 operations and near-instant settlement, as well as by reducing the number of financial intermediaries and the cost of post-trade processing. Tokenisation of assets and money, combined with smart contracts, allows for greater programmability and fractionalisation of assets, deepening existing markets, potentially unlocking new ones, and changing how capital assets are mobilised within the financial system.

However, without proactive intervention by central banks, there is a risk that the private sector adopts DLT in a way that delivers outcomes that undermine financial stability. Widespread adoption of public permissionless platforms for core functions could result in systemic vulnerabilities if the appropriate governance, risk management, and assurances for settlement finality are not in place to manage these risks. It is therefore important that the efficiency gains offered by this technology are not achieved at the expense of the resilience of the financial system. The Bank is actively engaging on DLT adoption by the private and public sectors and intervening where necessary to support its responsible adoption.

> **The FPC welcomes work by the Bank to propose a regulatory regime for sterling-denominated systemic stablecoins.**

The development of new financial products such as stablecoins and tokenised deposits present both opportunities and risks to the UK financial system. The FPC recognises the transformative potential of technology associated with stablecoins and the importance of ensuring that the public can have the same trust in new forms of money as they do in existing ones. It also notes the potential for growth in funding directly from financial markets and NBFIs to support the provision of credit to UK household and businesses, even if deposits move from the banking system to stablecoins. The FPC therefore takes action to support the responsible adoption of innovative technology by the financial sector, in line with its secondary objective (Section 1 and Box A).

In the UK, the Bank and FCA are developing regimes for systemic and non-systemic stablecoins to ensure appropriate resilience. Other jurisdictions, including the US, are also in the process of designing and finalising their regimes. The FCA consulted on their regime earlier this year, aimed at supporting the sustainable, long-term growth of crypto in the UK while delivering appropriate levels of market integrity and consumer protection.[35] In addition, the Bank has recently published a **consultation paper** on its proposed regulatory regime for sterling-denominated systemic stablecoins, and an accompanying **Financial Stability Paper** which sets out the role of holding limits for sterling-denominated systemic stablecoins and a potential digital pound. The FPC welcomes this work, recognising both the transformative potential of technology associated with stablecoins and that there is a risk of reduced lending to businesses and households as the economy adjusts to these new forms of money.

The FPC will also continue to monitor the interactions between stablecoins (including systemic stablecoins) and the wider financial system. Uptake of new stablecoin instruments in the UK could have consequences for other systemically important parts of the financial system. For example:

- Increased demand by stablecoin issuers for the short-dated government debt securities that back the stablecoins they issue could affect the structure and dynamics of that market. Similarly, asset liquidations by stablecoin issuers could have spillover effects on these markets.
- The widespread adoption of stablecoins for retail payments could result in bank disintermediation. This could arise in the transition to steady state – as digital money gains traction, deposits could migrate out of the banking system – with potential consequences for banks' provision of credit (both the quantity and terms) to the real economy. It could also happen in stress scenarios – for example, by providing another form of perceived 'safe haven' for depositors. This could amplify an initial stress, with potential implications for credit availability and resilience.

The Bank's proposed regime considers potential policy tools to mitigate these risks.

The FPC also supports international efforts to manage the risks posed by stablecoins. These include the FSB's **recommendations** on the regulation, supervision and oversight of global stablecoin arrangements, and **guidance** by the Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions. The FPC also supports further international work to understand potential risks from the issuance of multi-jurisdictional stablecoins and how best authorities can mitigate and manage them, including through co-operation in day-to-day supervision and at times of market stress.

> **The FPC are continuing to monitor developments in the unbacked cryptoasset sector and its interconnectedness with the financial sector and the real economy.**

Although DLT has promising potential to increase efficiency and reduce costs in financial markets, unbacked cryptoassets establish no claim on future income streams or collateral, meaning they have no intrinsic value. As set out in the April 2025 FPC Record, they have continued to grow in size and in interconnectedness with the financial system in recent years. For example, total global assets under management in crypto-based exchange traded funds have increased from $40 billion in 2022 to $190 billion in 2024.

Financial firms' activity in these markets has in part been limited by regulatory uncertainty: for example, global standards on the regulatory approach to banks' exposures are yet to be implemented. These standards aim to support bank resilience and financial stability. The implementation of regulatory frameworks around unbacked cryptoassets will provide clarity, and could in turn accelerate their adoption, including by banks who play a key role in providing vital services to the real economy.

The FPC will continue to monitor developments in the unbacked cryptoasset sector and its interconnectedness with the financial sector and the real economy.

7.3: Climate-related risks

Climate-related risks to financial stability are becoming more proximate.

In the **November 2024 Financial Stability Report**, the FPC set out a framework to help identify and assess climate-related risks to UK financial stability. Given the significant uncertainty around the magnitude of future climate-related financial losses and how soon they could crystallise, the FPC committed to further monitoring of climate-related risks and emphasised the importance of scenario analysis, including in the context of stress testing. This was also highlighted in the 2024 and 2025 **Remit and recommendations for the Financial Policy Committee**.

As set out in a recent speech by **Sarah Breeden**, there is increasing evidence that climate-related risks could materialise within the time horizons the FPC typically considers. This section considers risks to asset prices and credit quality which could – in a severe but plausible scenario – impact financial stability within the next five years, as well as risks to insurance coverage which are likely to develop over a longer time horizon.

If investors were to reprice financial assets rapidly to reflect climate-related risks, staff estimate that the resulting move in asset prices could be comparable to those moves seen in recent market stress episodes.

Previous Bank work has highlighted that climate-related risks are only partially priced into the value of corporate and sovereign bonds. As set out in **Sarah Breeden's** speech, climate-related risks could pose challenges to financial stability in the near term if investors suddenly priced in the costs of transitioning to net zero or the increase in physical risks resulting from persistently high emissions – known as a 'Climate Minsky Moment'.

Financial assets prices could be affected if investors priced in the expected impacts of physical and transition risk-focused scenarios on corporate and government debt sustainability, as well as the related macroeconomic impacts which could include higher inflation, interest rates, and risk premia. [36] In the transition risk-focused scenario, higher inflation associated with higher carbon prices and other climate policies leads central banks to raise policy rates, pushing down on the price of both corporate and government debt. Higher carbon prices also increase corporate credit risks due to higher costs and lower expected revenues for businesses. In the physical risk-focused scenario, losses are driven by the increased frequency and severity of extreme weather events as global temperatures rise, which would have a severe negative impact on GDP and corporate earnings.

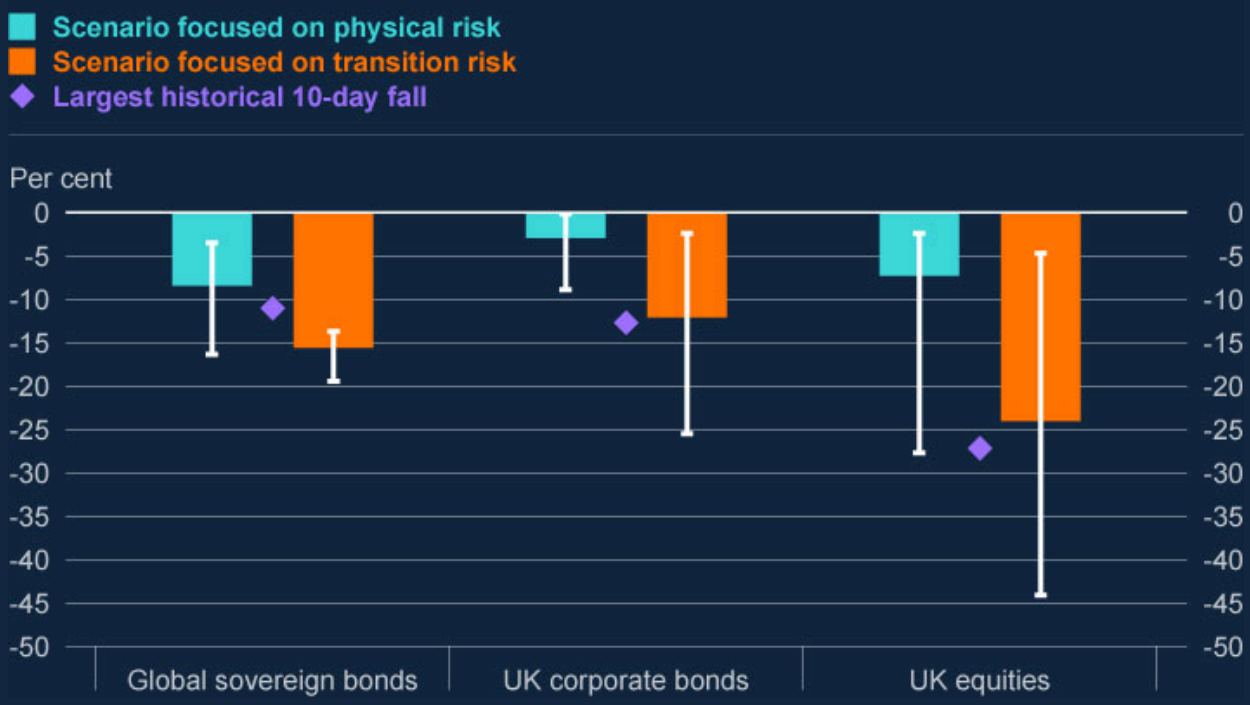
Staff estimates are based on the severe but plausible assumption that markets fully price in one of these two illustrative scenarios within a short period. But it is of course not possible precisely to estimate the likelihood of these scenarios occurring, nor the likelihood that a rapid repricing might occur.

If investors were to price the future impacts of these scenarios into today's asset prices, the resulting move in asset prices could be comparable to those moves seen in recent market stress episodes (Chart 7.1). For example, a severe macro shock associated with transition risks could lead to a 16% fall in government bond prices. This effect would be larger for countries with a

longer-dated maturity profile, shifting more of the interest rate risk from governments to investors. [37] The physical risk-focused scenario leads to a smaller fall in government bond prices of around 8%, largely because there is limited interest rate risk in the scenario used – even though the negative GDP impact of the physical risk-focused scenario is much larger than in the transition risk-focused scenario.

Chart 7.1: If investors were to reprice financial assets rapidly to reflect climate-related risks, the resulting move in asset prices could be comparable to those moves seen in recent market stress episodes

Per cent fall in asset prices relative to baseline under a 'Net Zero 2050' and 'Current Policies' scenario (a) (b) (c) (d)



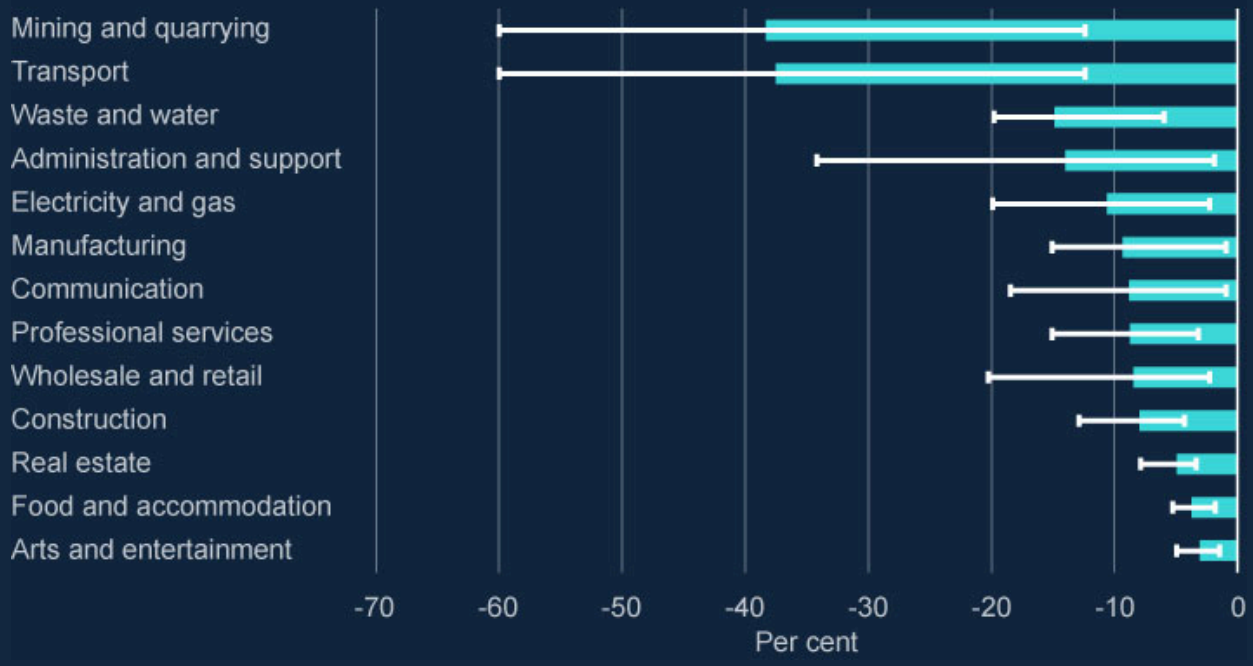
Sources: Bloomberg Finance L.P., MSCI ESG Research LLC, NGFS Phase V Scenario Explorer, Refinitiv Eikon from LSEG, World Bank and Bank calculations.

(a) The physical risk scenario is based on the NGFS 'Current Policies' scenario. The transition risk scenario is based on the NGFS 'Net Zero 2050' scenario. The estimates are based on pricing in the impacts of both scenarios out to 2050. These scenarios are subject to considerable uncertainty not reflected in this chart, and do not capture mechanisms such as environmental tipping points, compound risks, or social impacts such as migration. These mechanisms mean the impact of increases in global temperatures may be underestimated. The estimates of GDP losses associated with physical risk in NGFS scenarios are calibrated based on recent academic research, some of which has been subject to post-publication critique arguing risks are overestimated and is undergoing further peer review.
(b) 'Global sovereign bonds' is a portfolio of long-dated sovereign bonds of G7 countries. 'UK corporate bonds' are the stock of all corporate bonds issued by UK corporates, or those with a UK-based parent. 'UK equities' is the constituents of the FTSE All-Share index.
(c) The largest historical 10-day fall is the largest 10-day fall in the benchmark index since January 1998. Sovereign bonds are benchmarked against the historical performance of the Bloomberg 10+ Year Total Return Index Value Unhedged, in USD. The benchmark portfolio has a shorter average maturity than the modelled sovereign bond portfolio. UK corporate bonds are benchmarked against the historical performance of the ICE BofA Sterling Corporate High Yield and Investment Grade indexes. UK equities are benchmarked against the historical performance of the FTSE All-Share index.
(d) Error bars reflect the 10th and 90th percentile impacts within the relevant portfolio under each scenario.

Corporate bond and equity prices could also fall as these scenarios are priced in, with UK corporate bond prices falling by 12% and the FTSE All-Share index falling in value by around 24% under the transition risk scenario. These impacts would be particularly large for firms in sectors such as mining and oil and gas, which could be particularly affected by higher carbon prices and other climate policies (Chart 7.2). For example, corporate bonds issued by firms in the transport and mining and quarrying sectors could fall in value by as much as 60% as investors price in lower cash flows and higher costs related to transition policies. By contrast, firms in less energy-intensive sectors such as arts and entertainment and food and accommodation would see smaller falls in bond prices. The scenario would likely benefit other corporates with transition aligned business plans, including those which are not currently listed, or which have not issued corporate bonds.

Chart 7.2: Falls in asset prices related to transition risks would be largest in sectors particularly affected by higher carbon prices and other climate policies

Per cent fall in corporate bond prices under a 'Net Zero 2050' scenario, by sector (a) (b)



Sources: Bloomberg Finance L.P., MSCI ESG Research LLC, NGFS Phase V Scenario Explorer, Refinitiv Eikon from LSEG and Bank calculations.

(a) The transition risk scenario is based on the NGFS 'Net Zero 2050' scenario. These scenarios are subject to considerable uncertainty not reflected in this chart, and do not capture mechanisms such as environmental tipping points, compound risks, or social impacts such as migration. The physical risk estimates in NGFS scenarios are calibrated based on recent academic research, some of which has been subject to post-publication critique and is undergoing further peer review.
(b) Bars reflect weighted average falls of corporate bonds issued by UK corporates or corporates with a UK parent. Error bars reflect the 10th and 90th percentile impacts within the relevant sectors. Price falls shown in this chart capture increases in credit risk and impacts of interest rate paths in the scenario. Price falls are capped at 60%.

The financial stability impacts of this repricing, and the scale of losses borne by banks and NBFIs, would depend on the speed of adjustment. If the repricing were sudden – such as over the course of 10 days – it could be amplified by the responses of financial market participants, in line with the findings of the Bank's 2024 **system-wide exploratory scenario exercise**. For example, institutional investors could be required to sell corporate bonds if they were downgraded from investment grade to high yield or be forced to sell assets to meet liquidity needs from redemptions or margin calls on leveraged exposures. Such actions could increase the corporate bond price impact of the transition-focused scenario by around 4 percentage points.

These scenarios would increase borrowing costs for governments and businesses globally – and as such intensify pressures on sovereign bond markets (Section 2). Unless accompanied by other sources of stress, they would be unlikely to materially disrupt the provision of vital services to UK households and businesses. The likelihood of such a shock materialising could be mitigated if risk managers take actions early to understand and price their exposure to climate-related risks.

> **In addition, UK banks could face climate-related credit losses over coming years, particularly related to transition risks from sharp increases in energy and carbon prices.**

As well as market risks from sudden asset repricing, firms could also face climate-related credit losses on their lending to households and businesses. The Bank's **Climate Biennial Exploratory Scenario**, published in 2022, showed that UK banks could face material credit losses from their exposures to physical and transition risks, but there was substantial uncertainty around the magnitude of these risks.

A recent data collection by the Bank and the PRA shows the presence of climate risks in major UK banks' current wholesale and residential real estate exposures would lead to financial losses. Major UK banks provide substantial financing to agriculture-related activities, transportation including manufacture, and real estate.[38] These climate-sensitive sectors account for close to 23% of major UK banks' wholesale credit exposures, as measured by risk-weighted assets. And around 13% of major UK banks' lending to businesses and financial institutions is to sectors currently covered by Emissions Trading Schemes (ETSs). These businesses are vulnerable to increases in carbon prices, which can occur as a result of government policy, but also **in response to increases in gas prices**. Therefore, they are more highly exposed to transition-related cost headwinds which could adversely affect their ability to repay their debts.

Similarly, around half of banks' high loan to value (LTV) mortgage lending is to properties with Energy Performance Certificate (EPC) bands D or below. Banks could face losses on their lending secured on buy-to-let properties as an EPC rating of 'C' or above could become a minimum requirement for rentability as early as 2028. Further, households in less energy efficient properties are more exposed to sharp increases in energy prices, potentially affecting their ability to repay their mortgage debts. In aggregate, banks' exposures to losses from physical risks in the residential real estate portfolio appears to be more limited: only 5% of high-LTV mortgage

exposures are estimated to be at severe but plausible risk of a flood event. Losses to banks from flooding are also mitigated by the high availability of flood insurance, including due to the presence of Flood Re (more information below).

The credit quality of UK banks' lending is typically strong. Most UK mortgages have an LTV ratio below 70%, and the FPC's loan to income (LTI) flow limit provides protection against the UK household sector becoming overly indebted. Further, most bank lending to corporates is investment grade, and ETS allowances mitigate the impact of transition risks on some corporate borrowers. Taken together, these factors would mitigate the impact of any crystallisation of transition risks on banks' expected losses from these asset classes.

That said, the materiality of banks' exposures to climate-vulnerable counterparties underscores the need for such risks to be incorporated into banks' risk assessments and management capabilities, as set out in the PRA's **consultation paper** on climate-related risks. This would advance the PRA's primary objective to promote the safety and soundness of the firms that it regulates and would contribute to the resilience of the UK banking system as a whole. In improving the resilience of the financial system to climate-related risks, these improvements could also lead to a more stable medium-term growth path for the UK economy.

Climate-related risks to household and corporate lending may result in credit losses for banks within a five-year horizon. Bank staff will use the data collected to conduct further analysis on the materiality of transition and physical risks in banks' commercial real estate lending and trading books, as well as to inform whether and how such risks should be captured in future Bank Capital Stress Tests.

> **As physical risks from climate change continue to increase over the longer term, lower insurance coverage could transfer risks to households, businesses, banks and governments. Supporting insurability through investments in resilience to physical risks from climate change would be beneficial to UK financial stability.**

As set out in the **November 2024 Financial Stability Report**, the shorter-term financial impact of flooding on households is likely to be limited due to strong flood insurance coverage and affordability relative to other countries. This is in part due to Flood Re – a joint reinsurance initiative between the Government and the insurance industry, which promotes the affordability and availability of insurance for households at high risk of flooding.[39] Credit risks to banks from physical hazards are also currently mitigated by high insurance coverage.

But **recent estimates by the Environment Agency** suggest that the number of households at risk of flooding could increase from 6.3 million in 2024 to 8 million by 2050. Further, Flood Re is due to end in 2039 and has a statutory objective to manage the insurance market's transition to a post-Flood Re pricing model. Taken together, these changes could lead to decreases in insurance coverage due to insurers withdrawing from certain regions, or pricing becoming unaffordable for households. This could pose financial stability risks in the long term by negatively affecting:

- **Households** – through **lower house prices due to uninsurability and the costs of repair from physical damages** as well as difficulty remortgaging a property if there is a lack of available insurance.
- **Businesses** – through the destruction of physical goods, capital and infrastructure, as mentioned in a recent speech by **James Talbot**.
- **Economic growth** – through the direct impact of floods on consumption and inflation, and the indirect effects of lower insurance coverage on investment.
- **Banks** – through higher losses on lending to households and businesses affected by flooding. This impact would be particularly large on lower-quality or higher-physical risk portfolios.
- **Governments** – through the potential need to act as implicit or explicit insurers of last resort more frequently, including to support the economy during periods of stress caused by extreme weather events. The associated added strains on fiscal pressures that this would imply could further weigh on sovereign debt markets (Section 2).

All of these effects could impact the ability of the financial sector to provide financial services UK households and businesses.

Investment in physical resilience and actions to enhance financial resilience could be beneficial to UK financial stability by supporting insurability as physical risks increase. For example, collaboration between businesses, households and governments to facilitate investment in physical resilience – such as the **Flood Re Build Back Better** scheme – may reduce the financial impacts of extreme weather events. Updates to planning rules and building regulations could further mitigate the impact of increased physical hazards on UK households and businesses.

These risks also present an opportunity for collaboration between insurers, reinsurers and banks to develop innovative financial products to promote the pooling of risks and increase financial resilience – as recently highlighted by the **Climate Financial Risk Forum**. Actions to improve firms' climate-related modelling capabilities – such as those mentioned in the PRA's **consultation paper** on climate-related risks – should improve their ability to price and manage risks. As with operational resilience, a collaborative approach between authorities and the UK financial sector is essential to ensure resilience to climate-related risks, which is a prerequisite for sustainable economic growth.

Annex 1: Macroprudential policy decisions

This annex lists any FPC Recommendations and Directions from previous periods that have been implemented or withdrawn since the **July 2025 Report**, as well as Recommendations and Directions that are currently outstanding. It also includes those FPC policy decisions that have been implemented by rule changes and are therefore still in force.

Each Recommendation or Direction has been given an identifier to ensure consistent referencing over time. For example, the identifier 17/Q2/1 refers to the first Recommendation made at the 2017 Q2 Committee meeting.

Outstanding FPC Recommendations and Directions (as at the date of the FPC's meeting on 25 November 2025)

On 23 March 2023, the FPC made the Recommendation (23/Q1/2) that:

- The Pensions Regulator (TPR) should have the remit to take into account financial stability considerations on a continuing basis. This might be achieved, for example, by including a requirement to have regard to financial stability in its objectives, which should be given equal weight alongside other factors to which TPR is required to have regard. The FPC noted that in order to achieve this, TPR would need appropriate capacity and capability.

On 27 June 2025, the FPC made the Recommendation (25/Q2/1) that:

- The PRA and FCA should together (i) aim to ensure that the aggregate flow of new residential mortgages from mortgage lenders at loan to income ratios (LTIs) at or greater than 4.5 does not exceed 15% of total new residential mortgages, and (ii) allow individual lenders to increase their share of lending at such high LTIs while aiming to ensure the aggregate flow remained consistent with the limit of 15%. The FPC recognises that, in doing so, such high LTI lending by individual lenders could exceed 15% of their total number of new residential mortgages while the aggregate flow remains consistent with the 15% limit. The aggregate flow is calculated based on new residential mortgages extended by lenders which extend residential mortgage lending in excess of £150 million per annum.

The explanation of the Recommendation is set out in the **Record of the meeting on 27 June 2025**, and further discussed in Box A of this Report.

Other FPC policy decisions which remain in place

The following text sets out previous FPC decisions, which remain in force, on the setting of its policy tools. The calibration of these tools is kept under review.

Countercyclical capital buffer (CCyB) rate

The FPC agreed to maintain the UK CCyB rate at 2% on 25 November 2025, unchanged from its 2 October 2025 meeting. This rate is reviewed on a quarterly basis. The UK has also reciprocated a number of foreign CCyB rate decisions – more details are available at **The countercyclical capital buffer**. Under PRA rules, foreign CCyB rates applying from 2016 onwards will be automatically reciprocated up to 2.5%.

Leverage ratio

In September 2021, the FPC finalised its review of the UK leverage ratio framework, and issued a Direction and Recommendation to implement the outcome of the review as set out in its **October 2021 Record**.

In October 2022, in line with its statutory obligations, the FPC completed its annual review of its Direction to the PRA. The FPC revoked its existing Direction to the PRA in relation to the leverage ratio regime, and issued a new Direction on the same terms as in September 2021 with the addition of discretion for the PRA to set additional conditions to the central bank reserves exclusion.

The full text of the FPC's Direction to the PRA on the leverage ratio is set out in the Annex of the **October 2022 Record**, together with the original Recommendation (now implemented).

The PRA has **published its approach** to implementing this Direction and Recommendation.

Other FPC activities since the July 2025 Report

Other FPC activities since the July 2025 Report not included elsewhere in this Report include:

- Welcomed the commencement of the Bank Resolution (Recapitalisation) Act 2025 in July 2025. The Act introduced a new recapitalisation payment mechanism, primarily designed to facilitate UK small bank resolution if that was in the public interest. The FPC supported this targeted enhancement of the UK bank resolution regime which had helped to ensure the regime remains fit for purpose and ready for use.
- Finalised the **review of the O-SII buffer framework** in July 2025, confirming the FPC's decision to index O-SII buffer rate thresholds. As a result, the FPC reissued the O-SII buffer rates for 2024 to reflect this updated framework.
- In line with its statutory obligations, the FPC reviewed its Direction to the PRA on the leverage ratio, issued in September 2022. The FPC judged that the leverage ratio set out in the 2022 Direction should remain unchanged. Having regard to the interaction between monetary and macroprudential policy, the Committee confirmed the appropriateness of continuing to exclude central bank reserves from the leverage ratio, and of not recalibrating the minimum leverage ratio requirement of 3.25% to reflect an increase in reserves since 2016. The FPC would keep this under review as part of future reviews of the leverage ratio framework.

- Welcomed the publication of the PRA's near-final policy statement on **The Strong and Simple Framework: the simplified** capital regime for Small Domestic Deposit Takers (SDDTs) in October 2025. The FPC supports the policy to create a new Single Capital Buffer for SDDTs and to descope these firms from the CCyB and Capital Conservation Buffer (CCoB).
- Welcomed the results of the Bank's 2025 **Life Insurance Stress Test**, published in November 2025.
- Published a Financial Stability in Focus with further details on its updated assessment of the appropriate benchmark level of capital requirements for the banking system.

The **Financial Policy Committee Record – October 2025**, and **Financial Policy Committee Record – December 2025** contain more detail on the activities of the FPC since the July Report.

Annex 2: 2025 Bank Capital Stress Test: bank-specific results

The 2025 Bank Capital Stress Test assessed the resilience of the major UK banks and building societies against a severe negative global supply disruption that led to deep recessions across global economies. System-wide results are presented in section 5 of the FSR, while this annex provides complementary firm-level insights. The system remains resilient in the stress scenario. All participating banks maintain capital and leverage ratios above regulatory minima and continue to be able to support households and businesses through the stress. The tables below present the capital results for each participating bank.

The participating banks have differing business models, geographic footprints and capital starting positions which affect their results in the stress test.

- UK-focused banks – Lloyds Banking Group, Nationwide Building Society, NatWest Group and Santander UK Group Holdings plc were most affected by the UK macroeconomic stress, driven by higher interest rates, inflation, unemployment and house price falls.
- Internationally-diversified banks – Barclays plc, HSBC Holdings plc and Standard Chartered plc faced additional pressures from global downturns and traded risk shocks in markets such as Hong Kong, China, the US and Europe.

The results incorporate losses against the following key risk types:

- Credit impairments were the main source of losses for banks. The losses at the low-point year were lower than in the 2022/23 ACS, reflecting changes to the calibration of the scenario introduced in the 2025 Bank Capital Stress Test. It also reflects changes in asset quality and provisions taken against some international asset classes. Tables A3.1 to A3.4 contain projected impairments by bank.
- Several banks have material traded risk losses. Table A3.5 contains projected traded risk losses by bank.
- All banks incorporated stressed projections of misconduct costs and operational risk losses. Section 5.6 of the FSR contains further details.

The results also include a projection of how banks' RWAs will change in stress, based on changes in balance sheet size, the impact of the scenario, and firms' risk-weight models.

The impact of stressed losses is partly offset by the income that banks generate over the stress projection. The main source of income for participating banks is net interest income, which is affected by higher rates and pricing assumptions (Section 5.5 of the FSR contains further details).

Management actions played an important role in mitigating stress impacts. Banks included business-as-usual measures in their submissions, for example cost reduction actions. Banks also submitted Strategic Management Actions (SMAs) including reductions in lending and trading exposures, and further reductions in cost and distribution beyond business-as-usual measures. SMAs have been included in the banks' results where the PRC judged them credible, consistent with our guidance[40] and proportionate to the impact of the stress. No banks paid ordinary dividends up to the low point of the scenario (Table A2.2). Nationwide continued distributions on its Core Capital Deferred Shares throughout the stress.

The low points for CET1 ratios and leverage ratios after the impact of strategic management actions occurred in year 1 for all banks except Santander UK, for whom the low point occurred in year 2 for both ratios.

The PRC judged that this stress test did not reveal any capital inadequacies and that no bank is required to submit a revised capital plan.

Table A2.1: Projected CET1 capital ratios and Tier 1 leverage ratios in the stress scenario (a) (b) (c) (d) (e) (f) (g) (h)

Per cent	Actual (31 December 2024) including any remaining IFRS9 transitional	Actual (31 December 2024) excluding any remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
CET1 ratios						
Barclays	13.6	13.5	8.8	9.3	7.2	14.1
HSBC	14.9	14.9	10.8	11.9	5.8	14.5
Lloyds Banking Group	14.2	14.2	10.2	10.9	5.9	13.8
Nationwide	19.5	19.5	13.7	14.5	6.5	18.4
NatWest Group	13.6	13.6	11.1	11.1	6.0	14.2
Santander UK	14.8	14.8	9.7	10.3	6.9	14.3
Standard Chartered	14.2	14.2	8.6	9.8	6.1	14.2
Aggregate		**14.5**	**10.2**	**11.0**	**6.2**	**14.4**
Leverage ratios						
Barclays	5.0	5.0	4.0	4.2	3.25	4.9
HSBC	5.6	5.6	4.5	5.1	3.25	5.2
Lloyds Banking Group	5.5	5.5	4.4	4.6	3.25	5.2
Nationwide	5.2	5.2	4.6	4.8	3.25	5.2
NatWest Group	5.0	5.0	4.7	4.7	3.25	5.0
Santander UK	4.9	4.9	3.5	3.9	3.25	4.7

Per cent	Actual (31 December 2024) including any remaining IFRS9 transitional	Actual (31 December 2024) excluding any remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Standard Chartered	4.8	4.8	4.3	4.6	3.25	4.6
Aggregate		**5.3**	**4.4**	**4.7**	**3.25**	**5.0**

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(b) Tier 1 capital is defined as the sum of CET1 capital and Additional Tier 1 capital determined in accordance with the CRR.
(c) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a bank does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by PRA rules), Additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(d) Minimum aggregate CET1 capital ratios are calculated by dividing aggregate CET1 capital by aggregate RWAs at the aggregate low point of the stress in 2025. Minimum aggregate Tier 1 leverage ratios are calculated by dividing aggregate Tier 1 capital by the aggregate leverage exposure measure at the aggregate low point of the stress in 2025.
(e) The minimum CET1 capital ratios and leverage ratios shown in the table do not necessarily occur in the same year of the stress scenario for all banks. For individual banks, low-point years are based on their positions after any strategic management actions and automatic distribution restrictions. Minimum stressed ratio (before strategic management actions) corresponds to the same year as the minimum stressed ratio after strategic management actions.
(f) Low points for CET1 capital and Tier 1 leverage ratios occur in year 2 for Santander UK and year 1 for all other banks.
(g) The aggregate minima is calculated as a weighted average of minima in the aggregate low-point year.
(h) To produce aggregate results in a single currency, the Bank converts the results of HSBC and Standard Chartered – which report in US dollars – into sterling at a rate consistent with the scenario.

Table A2.2: Dividends, variable remuneration, AT1 coupons and other distributions in the 2025 Bank Capital Stress Test

£ billions	Dividends (a)		Variable remuneration (b)		AT1 discretionary coupons and other distributions (c)	
	12 months ending December 2024	To December 2025 in the stress	12 months ending December 2024	To December 2025 in the stress	12 months ending December 2024	To December 2025 in the stress
Barclays	1.2	0.0	1.1	0.0	2.8	0.7
HSBC (d)	9.1	0.0	2.1	1.4	12.8	2.1
Lloyds Banking Group	1.9	0.0	0.2	0.1	2.5	0.7
Nationwide (e)	0.1	0.1	0.1	0.0	0.1	0.2
NatWest Group	1.7	0.0	0.3	0.1	2.5	0.4
Santander UK	0.5	0.0	0.1	0.0	0.9	0.2
Standard Chartered (d)	0.7	0.0	0.9	0.2	2.4	0.8
Aggregate (f)	15.3	0.1	4.8	1.8	24.0	5.1

Sources: Participating banks' STDF data submissions, Bank analysis and calculations.

(a) Ordinary dividends paid in respect of the year up until the noted period end.
(b) Variable remuneration reflects current year upfront cash awards pre-tax, paid in respect of the 12 months up until the noted period end.
(c) Other distributions include preference share dividends, special dividends, share buybacks and other discretionary distributions, as applicable.
(d) HSBC and Standard Chartered figures have been converted to sterling using exchange rates consistent with the stress scenario.
(e) Dividend figures for Nationwide refer to distributions relating to its Core Capital Deferred Shares, a CET1 capital instrument.
(f) Aggregate is the sum of all firms with HSBC and Standard Chartered converted to sterling using exchange rates consistent with the stress scenario.

Barclays plc

Table A2.3: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	13.6%	13.5%	8.8% (c)	9.3%	7.2%	14.1%
Tier 1 Capital Ratio (d)	16.9%	16.9%	11.8% (c)	12.3% (c)		17.8%
Total Capital Ratio (e)	19.6%	19.5%	14.5% (c)	15.0% (c)		20.4%
Memo: Risk-Weighted Assets (GBP billions)	358	358	398 (c)	398 (c)		357
Tier 1 Leverage Ratio (a) (f)	5.0%	5.0%	4.0% (g)	4.2%	3.25%	4.9%
Memo: Leverage Exposure (GBP billions)	1,207	1,206	1,177 (g)	1,178 (g)		1,285

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

HSBC Holdings plc

Table A2.4: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	14.9%	14.9%	10.8% (c)	11.9%	5.8%	14.5%
Tier 1 Capital Ratio (d)	17.2%	17.2%	12.7% (c)	13.9% (c)		16.9%
Total Capital Ratio (e)	20.6%	20.6%	14.7% (c)	16.5% (c)		20.2%
Memo: Risk-Weighted Assets (USD billions)	838	838	897(c)	839 (c)		879
Tier 1 Leverage Ratio (a) (f)	5.6%	5.6%	4.5% (g)	5.1%	3.25%	5.2%
Memo: Leverage Exposure (USD billions)	2,571	2,571	2,507 (g)	2,304 (g)		2,841

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

Lloyds Banking Group

Table A2.5: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	14.2%	14.2%	10.2% (c)	10.9%	5.9%	13.8%
Tier 1 Capital Ratio (d)	16.6%	16.6%	12.4% (c)	13.1% (c)		15.7%
Total Capital Ratio (e)	19.0%	19.0%	15.2% (c)	15.9% (c)		18.6%
Memo: Risk-Weighted Assets (GBP billions)	225	225	241 (c)	242 (c)		232
Tier 1 Leverage Ratio (a) (f)	5.5%	5.5%	4.4% (g)	4.6%	3.25%	5.2%
Memo: Leverage Exposure (GBP billions)	674	674	682 (g)	683 (g)		705

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

Nationwide

Table A2.6: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	19.5%	19.5%	13.7% (c)	14.5%	6.5%	18.4%
Tier 1 Capital Ratio (d)	22.1%	22.1%	15.9% (c)	16.7% (c)		21.1%
Total Capital Ratio (e)	24.3%	24.3%	18.9% (c)	19.7% (c)		23.2%
Memo: Risk-Weighted Assets (GBP billions)	81	81	98 (c)	98 (c)		87
Tier 1 Leverage Ratio (a) (f)	5.2%	5.2%	4.6% (g)	4.8%	3.25%	5.2%
Memo: Leverage Exposure (GBP billions)	344	344	342 (g)	342 (g)		350

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

NatWest Group

Table A2.7: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	13.6%	13.6%	11.1% (c)	11.1%	6.0%	14.2%
Tier 1 Capital Ratio (d)	16.5%	16.5%	14.0% (c)	14.0% (c)		17.2%
Total Capital Ratio (e)	19.7%	19.7%	17.2% (c)	17.2% (c)		20.2%
Memo: Risk-Weighted Assets (GBP billions)	183	183	204 (c)	204 (c)		189
Tier 1 Leverage Ratio (a) (f)	5.0%	5.0%	4.7% (g)	4.7%	3.25%	5.0%
Memo: Leverage Exposure (GBP billions)	608	608	612 (g)	612 (g)		649

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

Santander UK Group Holdings plc

Table A2.8: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	14.8%	14.8%	9.7% (c)	10.3%	6.9%	14.3%
Tier 1 Capital Ratio (d)	18.0%	17.9%	12.8% (c)	13.6% (c)		17.3%
Total Capital Ratio (e)	20.9%	20.9%	15.7% (c)	16.5% (c)		19.9%
Memo: Risk-Weighted Assets (GBP billions)	67	67	67 (c)	65 (c)		69
Tier 1 Leverage Ratio (a) (f)	4.9%	4.9%	3.5% (g)	3.9%	3.25%	4.7%
Memo: Leverage Exposure (GBP billions)	242	242	245 (g)	226 (g)		255

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

Standard Chartered plc

Table A2.9: Projected consolidated solvency ratios in the stress scenario

Metric	Actual (31 December 2024) including remaining IFRS9 transitional	Actual (31 December 2024) excluding remaining IFRS9 transitional	Minimum stressed ratio (before strategic management actions)	Minimum stressed ratio (after the impact of strategic management actions)	Minimum requirements	Actual (30 September 2025)
Common Equity Tier 1 Ratio (a) (b)	14.2%	14.2%	8.6% (c)	9.8%	6.1%	14.2%
Tier 1 Capital Ratio (d)	16.9%	16.9%	11.1% (c)	12.6% (c)		16.7%
Total Capital Ratio (e)	21.5%	21.5%	14.4% (c)	16.4% (c)		20.3%
Memo: Risk-Weighted Assets (USD billions)	247	247	305 (c)	272 (c)		258
Tier 1 Leverage Ratio (a) (f)	4.8%	4.8%	4.3% (g)	4.6%	3.25%	4.6%
Memo: Leverage Exposure (USD billions)	868	868	794 (g)	735 (g)		937

Sources: Participating banks' published accounts and STDF data submissions, Bank analysis and calculations.

(a) The low points for the CET1 ratio and leverage ratio shown in the table do not necessarily occur in the same year of the stress scenario and correspond to the year where the minimum stressed ratio is calculated after strategic management actions. There is no conversion of banks' AT1 instruments in the stress.
(b) The CET1 capital ratio is defined as CET1 capital expressed as a percentage of the total risk exposure amount (risk-weighted assets or RWAs), where CET1 capital and RWAs are determined in accordance with the CRR.
(c) Corresponds to the same year as the minimum CET1 ratio over the stress scenario after strategic management actions.
(d) The Tier 1 capital ratio is defined as Tier 1 capital expressed as a percentage of RWAs, where Tier 1 capital is defined as the sum of CET1 capital and additional Tier 1 capital determined in accordance with the CRR.
(e) The Total capital ratio is defined as total capital expressed as a percentage of RWAs, where total capital is defined as the sum of Tier 1 capital and Tier 2 capital determined in accordance with the CRR.
(f) The Tier 1 leverage ratio is Tier 1 capital expressed as a percentage of the leverage exposure measure, as defined in Article 429(2) of the Leverage Ratio (CRR) part of the PRA Rulebook. If a firm does not have sufficient CET1 capital to meet 75% of the leverage ratio minimum requirement and 100% of its leverage ratio buffers (as required by the PRA rules), additional Tier 1 capital has been capped at 25% of the leverage ratio minimum requirement for the purpose of calculating the Tier 1 leverage ratio.
(g) Corresponds to the same year as the minimum leverage ratio over the stress scenario after strategic management actions.

Annex 3: 2025 Bank Capital Stress Test: bank-specific projected impairment charges and traded risk losses

Table A3.1: Projected cumulative five-year impairment charge rates on UK lending in the stress scenario (a) (b) (c)

Per cent	Mortgage lending to individuals	Non-mortgage lending to individuals	Commercial real estate lending	Lending to businesses excluding commercial real estate
Barclays	0.9	27.5	7.6	13.2
HSBC	0.5	18.2	8.0	8.2
Lloyds Banking Group	1.3	19.3	6.9	8.6
Nationwide	1.0	29.2	–	7.6
NatWest Group	0.9	29.2	7.9	7.4
Santander UK	1.0	19.4	5.5	11.7
Standard Chartered	–	–	–	10.3

Sources: Participating banks' Stress Test Data Framework (STDF) data submissions and Bank analysis and calculations.

(a) Cumulative impairment charge rates are the five-year total impairment charge divided by the average gross on balance sheet exposure, where the denominator is a simple average of 2024-28 year-end balance sheet positions.
(b) Portfolios with cumulative impairment charges of £0.0 billion or start point (2024 Q4) drawn balances of £0.0 billion (ie below £0.05 billion) are excluded.
(c) For the purposes of this table, the 'Nationwide' impairment charge figures equals the sum of Nationwide and Virgin Money UK heritage results pre-consolidation adjustments.

Table A3.2: Projected cumulative five-year impairment charges on UK lending in the stress scenario (a) (b)

£ billions	Mortgage lending to individuals	Non-mortgage lending to individuals	Commercial real estate lending	Lending to businesses excluding commercial real estate
Barclays	1.5	7.5	0.2	4.0
HSBC	0.6	2.7	0.5	6.8
Lloyds Banking Group	4.0	8.4	0.6	2.8
Nationwide	2.6	3.3	–	0.6
NatWest Group	1.8	5.3	0.7	4.5
Santander UK	1.6	2.0	0.2	1.1
Standard Chartered	–	–	–	0.3

Sources: Participating banks' STDF data submissions and Bank analysis and calculations.

(a) Portfolios with cumulative impairment charges of £0.0 billion or start point (2024 Q4) drawn balances of £0.0 billion (ie below £0.05 billion) are excluded.
(b) For the purposes of this table, the 'Nationwide' impairment charge figures equals the sum of Nationwide and Virgin Money UK heritage results pre-consolidation adjustments.

Table A3.3: Projected cumulative five-year impairment charge rates in the stress scenario (a) (b) (c) (d) (e)

Per cent	Lending to individuals					Lending to businesses				
	United Kingdom	Hong Kong and China	United States	Euro area	Rest of world	United Kingdom	Hong Kong and China	United States	Euro area	Rest of world
Barclays	4.6	–	35.3	–	–	12.7	–	19.2	9.6	11.7
HSBC	2.2	2.3	0.8	1.0	8.1	8.2	6.8	6.3	3.5	2.8
Lloyds Banking Group	3.4	–	–	0.7	–	8.2	–	8.7	–	6.4
Nationwide	2.1	–	–	–	–	7.5	–	–	–	–
NatWest Group	3.1	–	–	–	–	7.4	–	1.5	4.3	5.1
Santander UK	2.0	–	–	–	–	9.7	–	–	–	–
Standard Chartered	–	5.0	–	–	5.9	8.8	7.4	3.5	4.1	5.8

Sources: Participating banks' STDF data submissions and Bank analysis and calculations.

(a) Cumulative impairment charge rates are the five-year total impairment charge divided by the average gross on balance sheet exposure, where the denominator is a simple average of 2024-28 year-end balance sheet positions.
(b) Portfolios with cumulative impairment charges of £0.0 billion or start point (2024 Q4) drawn balances of £0.0 billion (ie below £0.05 billion) are excluded.
(c) Data exclude material associates.
(d) The table above is based on the country of residence of the obligor.
(e) For the purposes of this table, the 'Nationwide' impairment charge figures equals the sum of Nationwide and Virgin Money UK heritage results pre-consolidation adjustments.

Table A3.4: Projected cumulative five-year impairment charges in the stress scenario (a) (b) (c) (d)

£ billions	Lending to individuals					Lending to businesses				
	United Kingdom	Hong Kong and China	United States	Euro area	Rest of world	United Kingdom	Hong Kong and China	United States	Euro area	Rest of world
Barclays	9.0	–	9.0	–	–	4.2	–	2.1	0.6	0.4
HSBC	3.3	2.6	0.1	0.1	4.4	7.4	7.8	2.2	1.2	4.0
Lloyds Banking Group	12.4	–	–	0.1	–	3.5	–	0.2	–	0.1
Nationwide	6.0	–	–	–	–	0.6	–	–	–	–
NatWest Group	7.2	–	–	–	–	5.2	–	0.1	0.2	0.3
Santander UK	3.7	–	–	–	–	1.4	–	–	–	–
Standard Chartered	–	1.7	–	–	2.7	0.4	0.9	0.2	0.2	3.1

Sources: Participating banks' STDF data submissions and Bank analysis and calculations.

(a) Portfolios with cumulative impairment charges of £0.0 billion or start point (2024 Q4) drawn balances of £0.0 billion (ie below £0.05 billion) are excluded.
(b) Data exclude material associates.
(c) The table above is based on the country of residence of the obligor.
(d) For the purposes of this table, the 'Nationwide' impairment charge figures equals the sum of Nationwide and Virgin Money UK heritage results pre-consolidation adjustments.

Table A3.5: Projected traded risk losses 2025 of the stress scenario (a) (b)

£ billions	Projected losses
Barclays	-10.3
HSBC	-16
Lloyds Banking Group	-2.1
NatWest Group	-1
Standard Chartered	-5.3

Sources: Participating banks' STDF data submissions and Bank analysis and calculations.

(a) Traded risk losses include: market risk losses; counterparty credit risk losses, losses arising from changes in banks' credit and fair value adjustments; prudential value adjustment; gain/losses from fair value through other comprehensive income items and fair value options; excluding securitisation positions. They exclude banking revenues and costs.
(b) Nationwide and Santander UK are excluded as they have relatively minimal traded risk exposures.

Glossary

Abbreviations

ABS – asset-backed securities.

ACS – annual cyclical scenario.

AI – artificial intelligence.

AT1 – Additional Tier 1.

BBB – British Business Bank.

BTL – buy-to-let.

CAPE – cyclically-adjusted price-to-earnings.

CCoB – Capital Conservation Buffer.

CCPs – central counterparties.

CCS – Credit Conditions Survey.

CCyB – countercyclical capital buffer.

CET1 – Common Equity Tier 1.

CLOs – collateralised loan obligations.

CMORG – Cross Market Operational Resilience Group.

CNRF – Contingent NBFI Repo Facility.

CORST – Cyber and Operational Resilience Stress Test.

CRA – credit rating agencies.

CRE – commercial real estate.

CRR – Capital Requirements Regulation.

CTP – Critical Third Parties.

DC – defined contribution.

DLT – distributed ledger technology.

DSIT – Department for Science, Innovation and Technology.

DSR – debt-servicing ratio.

EMIR – European Market Infrastructure Regulation.

EMIR-TR – European Market Infrastructure Regulation trade repository.

EPC – Energy Performance Certificate.

ERP – equity risk premia.

ETS – Emissions Trading Scheme.

FCA – Financial Conduct Authority.

FMI – financial market infrastructure.

FPC – Financial Policy Committee.

FSB – Financial Stability Board.

FSR – Financial Stability Report.

FTSE – Financial Times Stock Exchange.

G7 – Canada, France, Germany, Italy, Japan, the United Kingdom and the United States.

GDP – gross domestic product.

GFC – global financial crisis.

GLEIF – Global Legal Entity Identifier Foundation.

GPT – General-Purpose Technology.

HGF – high-growth firms.

HMG – HM Government.

HM Treasury – His Majesty's Treasury.

ICE – Intercontinental Exchange.

ICR – interest coverage ratio.

IFRS – International Financial Reporting Standard.

IG – investment grade.

ILTR – Indexed Long-Term Repo.

IMF – International Monetary Fund.

IOSCO – International Organization of Securities Commissions.

IP – intellectual property.

LCD – Leveraged Commentary & Data.

LCR – liquidity coverage ratio.

LDI – liability-driven investment.

LL – leveraged loan.

LSEG – London Stock Exchange Group.

LTI – loan to income.

LTV – loan to value.

MA – Matching Adjustment.

MAIA – Matching Adjustment Investment Accelerator.

MBF – market-based finance.

MCOB – Mortgage Conduct of Business.

MiFID – Markets in Financial Instruments Directive.

MMF – money market fund.

MPR – Monetary Policy Report.

NAV – net asset value.

NBFI – non-bank financial institution.

NCSC – National Cyber Security Centre.

NGFS – Network for Greening the Financial System.

NIC – National Insurance Contributions.

OECD – Organisation for Economic Co-operation and Development.

OEF – open-ended fund.

OIS – overnight index swap.

ONS – Office for National Statistics.

O-SII – other systemically important institution.

OTC – over-the-counter.

PE – private equity.

PLR – Private Letter Rating.

PNFC – private non-financial corporation.

PPP – purchasing power parity.

PQC – post-quantum cryptography.

PRA – Prudential Regulation Authority.

PRC – Prudential Regulation Committee.

PTFs – Principal Trading Firms.

PtTB – price to tangible book.

RoTE – return on tangible equity.

RWA – risk-weighted asset.

SDDT – Small Domestic Deposit Taker.

SMA – Strategic Management Action.

SME – small and medium-sized enterprise.

SMF – Sterling Monetary Framework.

SMMD – sterling money market data.

STDF – Stress Testing Data Framework.

STR – Short-Term Repo.

SWES – system-wide exploratory scenario.

TFSME – Term Funding scheme with additional incentives for Small and Medium-sized enterprises.

TPR – The Pensions Regulator.

VC – venture capital.

VIX Index – Chicago Board Options Exchange Volatility Index.

YTD – year to date.

1. Refer to **Crafts (2004)**, **Crafts (2021)**, **Crafts and Harley (1992)**, **Crafts and Woltjer (2021)** and **Oliner and Sichel (2003)**.
2. Refer to **Fernald (2015)**, **Fernald et al (2017)**, **Fernald and Inklaar (2020)** and **Fernald et al (2025)**.
3. HGFs refer to scale-ups, firms with average annualised growth in employees or turnover greater than 20% per year over a three-year period, and with more than 10 employees in the beginning of the period, and high growth potential start-ups, young companies pursuing seed and start-up finance.
4. The corset was a mechanism that penalised banks for rapidly expanding their deposits, thus constraining the rate at which banks could increase their domestic lending. Refer to **McLeay et al (2014)** for a further explanation of how extending credit can increase deposits in the banking system.
5. The Magnificent 7 refers to seven large US technology companies: Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia and Tesla.
6. Also losses reported by Zions Bancorporation, Western Alliance Bancorp and BlackRock's HPS unit.
7. Underlying RoTE differs from statutory RoTE by excluding items such as restructuring costs and gains or losses on the purchase or sale of portfolios. Major UK banks' statutory RoTE in Q3 was 12.2%. One major UK bank did not publish full Q3 results. Aggregate Q3 indicators for the UK banking sector carried forward values from Q2 for that institution where data was unavailable.
8. A PtTB ratio above one indicates that investors expect RoTE to be above the level needed to compensate them for the perceived riskiness of those returns (referred to as the 'cost of equity').
9. The one-year forward price to earnings discount of UK banks relative to US banks is 30%, while the discount for other sectors is 36%. The analysis covers the largest five UK and largest five US banks. The discount for other sectors is for the FTSE 350 (excluding banks) relative to the US S&P 500 (excluding banks and information technology). The impact of the information technology sector on the S&P 500 has been stripped out, given its significantly larger impact on the US index than the UK.
10. **Letter from Charlotte Gerken and Laura Wallis 'UK Deposit Takers Supervision: 2025 priorities'**.
11. **Guidelines for counterparty credit risk management**.
12. Throughout this box, references to 'system-wide requirements' refer to aggregate capital requirements and buffers for the major UK banks, excluding firm-specific PRA buffers and requirements set by overseas authorities such as the international component of the CCyB. This reflects the significant role of the major UK banks in supplying vital services to the UK economy. Similarly, unless otherwise stated, aggregate figures presented in this box refer to an aggregate for major UK banks. Within the banking system, in practice, there will be a distribution of capital requirements reflecting individual banks' business models, their level of systemic importance, the degree of gaps and mismeasurement in their RWAs, and the PRA's view of firm-specific risks.
13. For example, **The Bank of England's approach to stress testing to the UK banking system**, the **policy statement on the Strong and Simple framework** and **PS22/25 on the Leverage Ratio**.
14. Hereafter referred to as 'banks'. The participating banks and building societies are: Barclays, HSBC, Lloyds Banking Group, Nationwide, NatWest Group, Santander UK Group Holdings plc and Standard Chartered.
15. In 2024 the Bank assessed the resilience of the banking system to two hypothetical scenarios in a desk-based exercise. **Financial Stability Report – November 2024**.
16. The results show that all participating banks would remain above the sum of minima and systemic risk buffers in the scenario.
17. The higher cost of living, which is particularly pronounced on vulnerable households, is estimated to increase impairments relative to the scenario starting point by 4% for mortgages and 20% for consumer credit. The impact for individual banks varies, reflecting the differences in their business models, lending portfolios and customer base. This is an improvement relative to the 2022/23 ACS, which reflects that households are more resilient due to increased real incomes as wage growth has outpaced inflation since the 2022/23 ACS and a lower inflation peak in this year's test.

18. In setting the CCyB the FPC uses a range of indicators that assess the level of financial vulnerabilities and the banking system's resilience to potential and actual shocks. This is outlined in **The Financial Policy Committee's approach to setting the countercyclical capital buffer**. As well as a view of the impact of a stress, the PRA buffer takes into account an assessment of risk management and governance alongside supervisory judgement. That supervisory judgement includes an assessment of any other relevant information. More detail is provided in **The PRA buffer – Prudential Regulation Authority Handbook and Rulebook**.

19. The impact of, and changes made to incorporate, IFRS 9 outlined in this document refers to banks participating in the Bank Capital Stress Test. The Bank is exploring the implications of the end of IFRS 9 transitional arrangements to the population of non-systemic banks and will communicate this in due course.

20. In 2019 the FPC raised the rate at which it expects to set the UK CCyB in a standard risk environment from 1% to 2%, alongside which the PRC implemented proposals to reduce minimum capital requirements in a way that left overall loss-absorbing capacity in the banking system broadly unchanged. This was intentionally not reflected in the stress-testing framework at the time as to do so would have resulted in a change in the PRC's risk tolerance.

21. **The PRA buffer – Prudential Regulation Authority Handbook and Rulebook**.

22. This includes the impact of judgements set out in Box 4 of **Stress testing the UK banking system: 2017 results**.

23. More information is included in **Key Elements of the 2018 Stress Test** and **The Financial Policy Committee's framework for the systemic risk buffer**.

24. The FPC's primary objective is to protect and enhance the stability of the financial system of the UK. Subject to that, the FPC's secondary objective is to support the economic policy of His Majesty's Government, including its objectives for growth and employment. The PRA's primary general objective is to promote the safety and soundness of PRA-authorised firms. The PRA has two secondary objectives to facilitate effective competition between firms and the international competitiveness of the UK economy.

25. Allocated business limits were used where committed limits were not disclosed.

26. Leveraged lending is defined as all types of loan or credit exposure where the borrower is majority-owned by a financial sponsor and/or the borrower's original post-financing leverage exceeds a total debt to earnings before interest, taxes, depreciation and amortisation ratio of four times.

27. This accounts for where the fund is managed. When looking solely at where the fund, and its assets, are domiciled, more than 90% of net gilt repo borrowing by hedge funds is in funds domiciled in the Cayman Islands. Where the hedge fund manager was reported in SMMD, Bank staff used GLEIF level 1 and level 2 data to identify the domicile of its managed funds.

28. This is discussed in more detail in a **recent speech by Lee Foulger**.

29. These were a sudden withdrawal of repo funding, liquidity stress from sharp increases in margin or collateral calls, stop loss or risk limit breaches, and cross-market or cross-border contagion.

30. Also losses reported by Zions Bancorporation, Western Alliance Bancorp and BlackRock's HPS unit.

31. Box 1.3 of the **IMF October Global Financial Stability Report**.

32. Preqin and Bank calculations.

33. For example, **Do private equity owned firms have better management practices**, Bloom et al, 2015.

34. On 28 November 2025, CME group suffered an outage across a number of its currency and futures markets, reported to have been linked to a cooling failure in a data centre. Services resumed later the same day, and impacts were limited due to it happening during a public holiday in the US. But the episode underscores the high interconnectivity of markets and the potential for operational failures in technology to cause disruption.

35. **Stablecoin issuance and cryptoasset custody**, and **Application of FCA Handbook for Regulated Cryptoasset Activities**.

36. The scenarios are based on the Network for Greening the Financial System's (NGFS's) 'Net Zero 2050' and 'Current Policies' scenarios. The former primarily reflects risks from a rapid transition to net zero carbon emissions by 2050, including high carbon prices and other climate regulations, and related higher inflation and interest rates. The latter focuses on physical risks from an increase in global temperatures to 2.5–3oC above pre-industrial averages, leading to higher intensity and severity of natural

disasters. These scenarios are subject to considerable uncertainty, and do not capture mechanisms such as environmental tipping points, compound risks, or social impacts such as migration. These mechanisms mean the impact of increases in global temperatures may be underestimated. The estimates of GDP losses associated with physical risk in NGFS scenarios are calibrated based on recent academic research, some of which has been subject to post-publication critique arguing risks are overestimated and is undergoing further peer review.

37. A longer maturity profile does provide a small benefit to investors in that the government continues to benefit from lower rates for longer before refinancing. This reduces governments' debt servicing costs, benefitting the fiscal position and reducing risk premia. But the effect of lower risk premia on bond prices is significantly outweighed by the increased duration risk.

38. Agriculture-related activities includes agriculture, fishing, and food and beverage manufacturing.

39. Flood Re is a reinsurance scheme that helps make the flood cover part of household insurance more affordable for households at high risk of flooding, by allowing insurers to cede the flood risk portion of policies to Flood Re for a fixed premium based on the property's Council Tax band.

40. **Stress testing the UK banking system: Guidance on the 2025 stress test for participants**.