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Banking is sophisticated, far more so than in 1988 when Basel I came in or even 2004 when Basel II agreed.

Individual exposures are assessed for return on capital – if capital required is too high relative to risk the bank won’t be able to price it to make a return and won’t transact

Eg requirement on income producing real estate in the UK under slotting very high

- EU bank requirement (where slotting not required) less than half UK banks’ requirement
- Recent data has shown that commercial property lending has moved out of UK banks

Banks are franchise players – insurance companies, PE houses and other non bank players are not.

If the going gets tough, the non franchise players will exit the market

Exacerbating cycles

Without experience of the markets mispricing of risk more likely

The Financial Services and Markets Act 2023 gave PRA a competition objective

But increasingly there seems to be a view that allowing new style banks to grow isn’t important – competition between the existing incumbents is enough

But the threat from the digital banks led to the clearers investing in digital

Some market segments not well served by the incumbents

£150bn of SME deposits held in deposits at zero interest – *Allica Bank Report October 2023*

And innovation is important

Not to give preferential treatment to challenger banks but to avoid penalising them

Over conservatism reduces the prospect for growth –capital backers have to see prospect of return on capital employed

Making the path to the capital treatments used by the clearers (models too slow) makes the gap impossible to bridge