Is Andrew Bailey the weakest link?

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The Financial Times has published an article by Andrew Bailey, governor of the Bank of England and chair of the Financial Stability Board, in which he warns of the risks posed by the explosive growth of private credit markets.

What struck me most about the piece was not what Bailey said. It was what he admitted without ever quite acknowledging the full implication of doing so. He suggested that the Financial Stability Board, which he chairs, has on its agenda:

[W]ork .... on mapping and defining the private finance ecosystem to tackle inconsistent definitions — speaking the same language is necessary if we are to have effective oversight.

Just consider what that means. Bailey is admitting that a financial market that may now be worth between $1.5 trillion and $2.5 trillion globally has emerged in plain sight since 2008, and yet the people supposedly responsible for maintaining financial stability still cannot properly define what it is.

That is extraordinary. This is not some marginal financial innovation operating in the shadows. This is now a core part of global finance. It is deeply interconnected with banks, insurers, pension funds, private equity, and asset managers, yet Bailey is telling us that regulators are still trying to work out the vocabulary to describe it before they can even consider what to do about it. If that does not sound alarm bells at this moment that we face economic crisis, it should.

First, this is a staggering regulatory failure. The job of central bankers and financial regulators is supposedly to identify systemic risk before it creates a crisis. Instead, they once again appear to have stood aside whilst financial engineers constructed another opaque, highly leveraged and poorly understood market whose risks are spread throughout the global economy.

We have, of course, seen this before. The language Bailey uses is eerily reminiscent of the years before the crash of 2008. Then, too, we were told that diversification

increased resilience. Then, too, we were told that innovation improved credit allocation. Then, too, regulators admitted, far too late, that they did not understand the interconnections embedded within the system. And then the whole thing blew up.

Second, Bailey's article unintentionally reveals the intellectual bankruptcy of modern financial regulation. Regulators have spent decades promoting deregulation, market liberalisation and "innovation" whilst simultaneously assuming that markets could self-correct. Private credit is the inevitable consequence.

Banks faced tighter regulation after 2008, so lending migrated into less regulated spaces. Predictably, vast amounts of capital flowed into opaque investment structures promising higher yields. Equally predictably, regulators chose not to interfere too much because markets were supposedly efficient and sophisticated investors supposedly knew what they were doing. Now Bailey admits the resulting structures are opaque, poorly valued and potentially impossible to manage in a crisis. That is not reassuring.

Third, the timing could hardly be worse. Bailey himself notes the growing risks: geopolitical instability, slowing growth, higher debt-servicing costs and the disruptive impact of AI. These are not hypothetical concerns. They are current realities.

Private credit has never been tested by a genuinely severe global downturn combined with sustained high interest rates. Nobody really knows what happens when large numbers of borrowers fail simultaneously in these markets. Nobody knows how quickly supposedly illiquid assets will collapse in value once investors attempt to exit. Nobody knows how far contagion might spread through insurers, pension funds and banks. And the reason nobody knows is precisely because the regulators failed to insist on transparency before allowing this market to grow to systemic scale.

That is the critical issue here. Regulation is not supposed to arrive after markets become dangerous. It is supposed to exist before danger emerges. Instead, Bailey is effectively telling us that the authorities are now scrambling to understand a market after it has already become systemically important. That is not prudence. It is negligence.

There is another issue embedded within this discussion. Private credit exists in large part because mainstream banking has failed to fulfil its social purpose. Banks increasingly prefer mortgage lending, speculative asset finance and wealth management because those activities generate lower-risk returns. Productive businesses, especially smaller firms, have increasingly struggled to obtain conventional finance. Into that vacuum stepped private credit funds.

But these funds are not public-interest institutions. They are yield-seeking vehicles operating largely for the benefit of wealthy investors. Their objective is not economic resilience, social need or productive transformation. Their objective is return maximisation. As a consequence, systemic financial fragility has once again become

profitable. And regulators let it happen.

The truly worrying issue is that Bailey seems to believe that better definitions, more information sharing and improved data collection might solve the problem. They will not. Transparency matters, of course. Definitions matter. But if a market structure is inherently fragile because it depends upon leverage, opacity, maturity mismatches and speculative yield-seeking, then documenting the problem does not remove the danger.

What is required instead is a willingness to intervene before a crisis occurs, if that is now possible. That means limits on leverage. It means mandatory transparency. It means proper capital requirements. It means strict regulation of interconnected exposures. It probably also means asking whether large parts of private credit activity should exist at all. Most of all, it means recognising that financial stability is not compatible with allowing vast pools of largely unregulated capital to grow unchecked simply because they are profitable.

Bailey ended his article by warning that “we are only as strong as our weakest link”. He is right. The problem is that he appears not to realise that the weakest link may well be the regulatory system he represents. Perhaps most worrying is that, for failing to spot that link, Andrew Bailey might be the weakest link of all.