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UK banks passed their stress tests with aplomb, but consumers weren't as lucky

Article

The news: The UK's eight largest banks have sufficient capital to withstand a crisis more severe than the Great Recession, per the Bank of England's annual bank stress test results.

Banks would also be capable of supporting consumers and businesses throughout this scenario.

The report card: The stress tests used data on banks' balance sheets as of June 2022. Since then, major UK banks' capital ratios have risen 0.4 percentage points to 14.6% in Q1 2023

- The tests factored in severe yet plausible economic shocks: a base bank rate of 6%, a 31% fall in residential real estate prices, unemployment more than doubling to 8.5%, and UK GDP contracting 5%.
- Under this scenario, aggregate loan losses could hit **£125 billion ($154 billion) throughout the five-year span** from June 2022. This would translate to an aggregate CET1 ratio of 10.8%, well above the passing rate of 6.9%.

The tests covered **Barclays**, **HSBC**, **Lloyds**, **Nationwide**, **NatWest**, **Santander**, **Standard Chartered**, and **Virgin Money**. These eight banks account for roughly 75% of lending to the UK economy, per Bloomberg.

Bank strength doesn't equal consumer health: A typical mortgage holder coming off a fixed-rate deal in 2023 will face a £220 ($271) increase to their monthly mortgage payments —and by the end of 2026, nearly 1 million homeowners will face £500 ($616) increases, per the BOE results. Renters would also suffer as landlords pass on higher mortgage rates to them.

- **Banks need to do more to support consumers—and stress tests prove they can.** BoE Gov. Andrew Bailey urged lenders to pass on higher interest rates to savers given their resilience, per The Financial Times.
- **This compounds prior FCA and MP calls for banks to do more.** UK lenders have been accused of profiteering from higher interest rates after their Q1 banks results. Lloyds' pre-tax profits jumped 46%, while NatWest's profits lept 50%, for example. Interest rates for easy access accounts, meanwhile, are largely stuck below 2%.

Our take: **Banks that offer better value can win big on deposits.**

- More than a half-million UK consumers switched banks between January and May 2023—**a 73% jump from a year ago**—as they hunt for better deals.
- Consider **Chase**: It already holds **£15 billion ($18.5 billion) in customer deposits**, after launching in the UK two years ago. But **Monzo** has accumulated just £6 billion ($7.4 billion)

since its 2015 rollout. Why? Because Chase offers 1% interest in its current account, 1% cash back on everyday spending to those who deposit over £500 ($616) a month, and a market-leading **3.8% interest for its easy access savings account**.

Offering similar rates would mean significantly higher cost of funds for the average UK bank. Instead of doing this across the board, UK banks can target certain demographics—like those who are likely to use other banking products—with their best offers. This would also help them create sticky relationships that won't be severed as soon as a better rate comes along.