



Trading Book Capital: Basel III Implementation and Latest Industry Trends
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Introduction and Welcoming Remarks
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Good afternoon, and welcome to ISDA's annual Trading Book Capital event – thanks for joining us today, and thank you to Deloitte for sponsoring.

This event has become an annual fixture in the ISDA calendar, and you may have noticed that it nearly always takes place in early December. When the days are at their shortest, the cold is beginning to bite and the Christmas lights are turned on, thoughts are turning to 2026 – plans, hopes and dreams.

As I prepared these remarks, I was thinking about what we in ISDA's Risk and Capital team are dreaming of for next year. I'm sure that if Mariah Carey were to remix her 1994 classic, she could think of no punchier lyrics than these: "I don't want a lot for Christmas... I just want an appropriate, risk-sensitive capital framework".

While I'm thankfully not planning a career move into festive musical remixes, I do want to talk briefly about why we're doubling down on our commitment to appropriate, risk-sensitive capital requirements as we move into 2026.

Healthy economies and successful companies rely on deep and liquid markets to access funding, hedge their risks and build resilience to withstand external shocks. If banks are hit with disproportionate capital requirements, their ability to provide liquidity will be impaired and economic growth will be constrained. That's why we'll continue to advocate for an appropriate capital framework around the world.

For the major jurisdictions that have still to complete the implementation of Basel III, it's clear that 2026 is going to be a crunch year. In the US, regulators are revising the Basel III endgame proposal in response to industry feedback, and we expect to see a new proposal in the coming months.

In the EU, the European Commission launched a targeted consultation last month on changes to the Fundamental Review of the Trading Book (FRTB) that would bring some short-term relief in key areas. These would include a set of temporary adjustments to the standardized and internal models approaches and the application of a multiplier, which negatively affected banks could use to limit the increase in their capital requirements for three years. As a general principle, we think long-term solutions are needed to ensure lasting risk sensitivity, rather than relying on temporary

measures. The consultation closes on January 6 and we're working with our members to develop a response.

Here in the UK, the Basel 3.1 framework is due to be implemented at the start of 2027, although the Prudential Regulation Authority has proposed delaying the rollout of internal models until the following year.

This brings me to the reduced viability of internal models under the FRTB, which we think should be a major concern for policymakers. Last year, we undertook a survey that showed only 10 out of 26 banks plan to use internal models for a reduced scope of trading desks under the FRTB. That's a big change that we don't think is in line with what the Basel Committee originally intended. Such a big shift away from internal models could lead to herd behavior and drive concentrations in particular assets. It will mean less diversity in models and less alignment between risk and capital – a direct contradiction of Mariah's hopes for Christmas.

We've recommended changes to improve the incentives to use internal models, which would require the recalibration of some parts of the FRTB, including the profit & loss attribution test, the risk factor eligibility test and non-modellable risk factors. The good news is that we've had positive engagement with policymakers on these issues, particularly in the US. There is still work to be done to ensure the viability of internal models, but we're hopeful that revisions to the Basel III endgame will include positive changes in this area.

Whether banks use standardized approaches or internal models, it is critical that those capital models are implemented accurately and consistently. That's why ISDA developed its Capital Models Benchmarking initiative, which has enabled firms around the world to implement and validate regulatory capital models with an unparalleled level of efficiency, accuracy and consistency. Originally designed for the standardized approach, this initiative has now been extended to support internal models and we'll hear more on that later this afternoon.

As market participants have navigated a series of unexpected shocks in recent years, they've also recognized the need to prepare for future climate-related shocks. In particular, the possible impact of natural disasters or changes in climate policy on traded assets hasn't historically been an area where firms have been able to lean on established best practice.

That has now started to change, thanks to ISDA's conceptual framework for climate scenario analysis in the trading book and the follow-up work we've done to design and model specific scenarios. This year, ISDA has produced market risk shocks associated with the short-term scenarios developed by the Network for Greening the Financial System and we'll publish a new paper on this early next year. Like ISDA's benchmarking initiative, our climate scenario analysis framework is a mutualized solution that responds to a shared industry challenge. We look forward to further advancing both services in the years ahead.

I hope these remarks have given a sense of why ISDA's hopes for next year are consistent with what we have always strived for. Risk-sensitive capital might not scan seamlessly into the lyrics of a classic festive tune, but it really is all we want for Christmas.