



Frenemies at the gates | Principal Trading Firms

Highlights from Rebecca Jackson's Keynote
Speech

February 2026



A changing market landscape and the growth of Principal Trading Firms

On 2nd February 2026 Rebecca Jackson, Executive Director Authorisations, Regulatory Technology and International Supervision gave a speech focused on changes to market structures, powered by technological innovations and the growing role of market participants such as PTFs.



Changing Market Landscape

Advances in New Technologies



Equity market conditions and prime brokerage

- Rising equity valuations have boosted prime financing balances, which strained funding capacity and widened wholesale equity financing spreads, prompting new participants to enter the market.
- Over the past year, equities have continued to hit new records despite bouts of volatility, with banks' prime brokerage balances reaching new peaks and the S&P 500 rising a further 16%, again led by mega-cap technology stocks.

Ongoing concerns about an AI-related equity bubble

- Regulatory authorities are closely monitoring the risks and potential consequences for banks if there is a sharp sell-off in risk assets, if such an event were ever to happen.

Shift of proprietary trading risk from banks to non-banks

- The proprietary trading risk that bank regulations aimed to contain has, in effect, migrated to the non-bank sector.

Risk has shifted form, not disappeared from banks

- Although proprietary market risk was pushed out of banks by post-crisis reforms, it has re-entered indirectly as counterparty risk to PTFs.
- PTFs depend on banks' balance sheets and credit standing to:
 - Use banks' trading infrastructure for executing and settling trades in listed derivatives and cash equities.
 - Conduct OTC FX spot and derivatives trades.
 - Clear trades via banks acting as general clearing members at CCPs, including trades executed away from the bank's own platforms.
 - Obtain financing via prime brokerage and repo for both intraday and end-of-day positions.

Technological advances in trading

- Rapid progress in technologies such as generative AI is transforming markets with further potential from technologies such as quantum computing.

- Market participants are increasingly using AI and machine learning for trading edge, while advances in trading infrastructure have slashed execution and transmission times from milliseconds to microseconds and even nanoseconds.

Structural changes in market participants

- After the Global Financial Crisis, regulation drove banks away from proprietary trading toward more client-focused business models.
- NBFIs—especially electronic market makers and ultra-low-latency Principal Trading Firms—stepped in as key liquidity providers in vanilla products, with some now earning trading revenues on par with major global investment banks.

PTFs increasingly resemble hedge funds in some activities

Many PTFs have moved beyond pure intraday market making into:

- Quantitative, hedge fund-like strategies with longer holding periods.
- Acting as “risk recyclers” for banks, taking on larger or more complex positions.
- Their overnight portfolios, financed by prime brokers, now have risk profiles similar to hedge funds.

Consequently, banks should apply the same risk measurement and risk management frameworks to PTF clients as they do to hedge fund clients in their prime brokerage businesses



“Frenemies” relationship between banks and Principal Trading Firms (PTFs)

- Even though major investment banks shuttered traditional prop trading desks but still act as market makers.
- As trading has gone electronic, PTFs now directly compete with banks in principle-based markets (e.g., FX, credit), where banks historically dominated through balance-sheet capital.
- In agency/commission markets (e.g., cash equities, equity ETFs), PTFs have largely displaced banks as the main market makers on exchanges.
- Despite this competition, PTFs rely heavily on banks for leverage, clearing, treasury and payments services, and market access.
- Banks and PTFs are therefore both competitors and clients—“frenemies”—and some PTFs have become highly valuable bank clients as they've grown.

What the increased risks may mean for exposed Banks

Challenges with PTFs and implications on Banks

Growth in Intraday Exposure

- Banks now face very large, fast-moving intraday counterparty exposures to Principal Trading Firms (PTFs), because they effectively guarantee settlement on the huge volume and velocity of PTF trades.
- As PTF activity and execution speed have grown, these intraday risks for banks have increased correspondingly.

Limitations of Current Pre-Trade Controls

- When PTFs route orders via bank platforms, banks can enforce automated pre-trade limits that block trades beyond their risk appetite.
- But when PTFs trade directly on venues or via bilateral arrangements, banks' pre-trade controls are often bypassed, leaving banks dependent on venue gateway limits, PTFs' own controls, and contractual exposure caps—which can be crude (not risk-sensitive), over-allocated, patchy, or even absent.

Reliance on Slow-Post Trade Monitoring

- Since pre-trade control coverage is incomplete, banks must rely heavily on post-trade data (“drop copies”) from CCPs, venues, and brokers to aggregate client exposures.
- This aggregation can take seconds to minutes (or even hours in some markets), while human intervention is slower still, creating a dangerous “response gap” versus trading that occurs in micro- or nanoseconds and could be driven by a malfunctioning algorithm.

Using “kill switches” in fragmented, high-speed environment

- If a problem is detected when PTFs trade through a bank's own channels, the bank can instantly stop all order flow (“kill switch”).
- When PTFs trade directly on multiple venues, banks must rely first on the PTF to act; if a bank detects the issue first, it must contact the PTF and/or coordinate remote kill switches across venues—costly in time and potentially allowing many more unwanted trades for the bank.

Potential for Large Losses and Recovery Risk

- In certain situations, a bank may be obligated to settle a large volume of erroneous or loss-making trades and only afterwards attempt to unwind positions.
- If markets move adversely, the bank bears significant losses upfront and then must seek recovery from the PTF, exposing it to substantial counterparty and collection risk.

Low probability but high impact Op/Technology Risk

- Although PTFs are regulated, technologically sophisticated, and capable of strong in-house pre-trade controls, the combination of speed, complexity, and cyber risk means catastrophic failures—though rare—remain plausible.
- Past incidents demonstrate that simple technology or process failures can trigger major market disruption and large losses, so banks must treat “rogue algo” scenarios as real, not hypothetical.

What Banks Need to Do?



Enter and grow in this business only with advanced risk infrastructure in place



Upgrade intraday counterparty risk measurement and aggregation



Map and strengthen pre- vs post-trade controls



Prepare for growing complexity and cross-product netting



Apply robust client due diligence and disclosure standards to PTFs



Assess clients' operational and technology risk controls



Ensure board-level awareness, oversight, and investment



Expect heightened supervisory scrutiny, the PRA is clear that it will focus on banks' counterparty exposures to PTFs in 2026

Thank you

For additional information and how we can help you, please contact:



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