"Rethinking Regulations in an Interconnected Financial System"[1]

Participants of the 'Management Development Programme on Financial Market Regulations', Professors, ladies, and gentlemen. A very good morning to all of you!

2. At the outset, I would like to thank IIM, Kozhikode for inviting me here. It is a pleasure to address such a diverse gathering, ranging from policy veterans to important stakeholders across the financial landscape. The contents of programme span the issues around the regulatory framework of a diverse mix of entities operating in the financial markets including banks, securities firms, and insurance entities.

3. Financial markets span a wide array of products starting with money markets, G Secs, forex, equities, commodities, and derivatives. These products are traded bilaterally, over the counter, or increasingly on electronic trading platforms or on exchanges. The entities are diverse, and they are active in many of these markets. They are regulated by different regulators depending on the nature of entities and/or their activities. The markets are interconnected with spillover risks from one set of market activities into another, increasingly becoming a point of concern from the point of view of financial stability. In my remarks today, I would like to, therefore, share a few perspectives on the need for market and entity regulations and their interplay, the tools employed by the regulators and the challenges faced in framing regulations for a rapidly evolving and interlinked financial ecosystem; and conclude by sharing a few thoughts on the way forward.

The role and evolution of financial sector regulations in India

4. To set the stage, it is essential to start by tracing the evolution of financial sector regulations in India, which commenced with the establishment of the Reserve Bank of India (RBI) in 1935. The Bank's remit was expanded in 1949 to cover regulation and supervision of commercial banks[2]. This was succeeded by empowering it to regulate and supervise non-banking institutions[3] now commonly referred to as Non-Banking

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[1] Inaugural Address delivered by Shri M Rajeshwar Rao, Deputy Governor, Reserve Bank of India – August 18, 2025 - at the DoPT MDP on Financial Market Regulations at the Indian Institute of Management Kozhikode (IIMK). Inputs provided by Chandni Trehan Saluja and Nilesh Dnyanoba Gawade are gratefully acknowledged.

[2] https://rbi.org.in/web/rbi/about-us/by-chronology

[3] Act 055 of 1963: Banking Laws (Miscellaneous Provisions) Act, 1963 (https://www.casemine.com/act/in/5a979d964a93263ca60b70c7)

Financial Companies (NBFCs) in 1964[4] and thereafter Urban Co-operative Banks (UCBs) in 1966[5].

5. The year 1991 is extremely significant as it ushered in key economic reforms which helped to transform and grow our economy. The reforms in the financial sector started in a way, with the implementation of the recommendations of the Narasimham Committee on financial sector reforms. The entry of private banks, introduction of prudential norms for banks, and alignment of capital adequacy requirements with global standards based on the recommendations of the Committee and conferring of statutory powers to the Reserve Bank to exercise greater oversight over the NBFCs were important policy landmarks during this period. This together with the subsequent changes in the monetary policy framework[6], the liberalisation of the exchange control regime and the grant of powers to regulate the Payment and Settlement Systems as well as the money, foreign exchange, and government securities (G-Sec) markets to the Reserve Bank, have collectively influenced the changes in the approach to regulation making at the Reserve Bank.

6. The Securities and Exchange Board of India (SEBI) was statutorily entrusted with regulation and development of the securities market in the year 1992[7]. The subsequent decades saw establishment of new financial sector regulators in the form of the Insurance Regulatory and Development Authority of India (IRDAI) to oversee the regulation of the insurance and reinsurance sectors and of the Pension Fund Regulatory and Development Authority (PFRDA) for pension funds. More recently in 2020, the International Financial Services Centres Authority (IFSCA) was created to regulate and promote financial products, services, and institutions within India's International Financial Services Centres. Collectively, these regulators play a critical role in the journey of transforming India's financial system into a more resilient, market-driven, and consumer-centric ecosystem, while facilitating sustainable economic growth of the country.

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[4] Chapter IIIB of RBI Act, 1934.

[5] https://rbi.org.in/web/rbi/about-us/by-topics/brief-history-of-urban-cooperative-banks-in-india

[6] From abolishing to automatic monetization through ad-hoc T bills to Multiple Indicators approach from 1998 to 2009, followed by a transition period with pre-conditions to kick in inflation as the nominal anchor guided the monetary policy from 2013 to 2016 and, thereafter, the Flexible Inflation Targeting framework: https://rbi.org.in/web/rbi/-/speeches-interview/seven-ages-of-india-s-monetary-policy-1092

[7] SEBI was established in 1988 as a non-statutory body for regulating securities market.

Approach for Regulation making

7. The market-oriented *laissez-faire* approach towards Regulation of financial markets with minimal regulations operates on the assumption that self-regulation will be effective. However, this view has been contested by some economists and policymakers who argue that regulation is not just necessary but essential. They contend that the idea of inherently self-correcting markets is more of an ideological fad than a factual occurrence, and that effective oversight is crucial to ensure stability, transparency, and protection of the financial sector against systemic risks. Nobel Laureate Joseph Stiglitz in his influential book *Freefall: Free Markets and the Sinking of the Global Economy* writes, "*The crisis has made it clear that self-regulation – which the financial industry promoted and which I view as an oxymoron – doesn't work*." Time and again it has been proven that financial regulation is essential not only to prevent market failures, but also to protect consumers and safeguard the stability and resilience of the broader economy, particularly in times of crisis. The common misconception that regulation inherently imposes restrictive barriers, is inaccurate. A well-designed financial oversight framework underpinned by thoughtfully crafted regulations not only ensures a level playing field but also fosters sustainable growth and development.

How do we regulate financial systems[8]

8. Before delving into the specific approaches to regulation-making, it is important to first reflect on the broader frameworks for financial system regulation, especially considering that alternative models of financial oversight are in vogue.

9. The regulatory oversight architecture for financial systems can be broadly categorised into **three main models**. The first model is known as '**sectoral or traditional model'**, in which each of the financial sector authorities is responsible for both - prudential and conduct aspects of the specific financial sector, i.e., banking, insurance, securities and market integrity. This approach has been followed by countries like India, Brazil, Hong Kong and Mexico and remains the most commonly used model around the world. However, challenges arise in such a model while dealing with financial conglomerates, whose activities blur the boundaries between

[8] https://www.bis.org/fsi/publ/insights8.htm and https://www.researchgate.net/publication/290574692_Approaches_to_Financial_System_Regulation_An_International_Comparative_Survey

different types of financial institutions. Such trade-offs can be smoothed by introducing complementary arrangements, like those adopted by Indian Financial Sector Regulators (FSRs), which I will discuss later.

10. An alternative approach is the '**integrated model'**, where a single agency oversees all oversight functions including regulations across the finance industry. This model was adopted by Singapore in 1984 as a consequence of reforms in financial oversight architecture. Later Scandinavian countries adopted similar models, followed by the UK, which established a single Financial Services Authority (FSA) in 1997. Further, countries like Russia, Japan, Germany and South Korea have adopted this model in their financial architecture. While this approach offers a cohesive and streamlined framework for overseeing the financial sector, enabling unified decision-making, reduced regulatory arbitrage, and improved co-ordination, it may present some operational challenges like risk of possible single point of regulatory failure, dilution of sectoral focus and reduced flexibility in addressing the needs of different sub-sectors.

11. The third model involves grouping responsibilities either according to regulatory and supervisory goals or according to sectors, i.e., **partially integrated approach**. The '**Twin Peaks**' model is an example of this, where two separate agencies manage each of the prudential oversight and conduct of business for all types of financial institutions. This model was first adopted in Australia in 1997, followed by Netherlands in 2002 and thereafter introduced in Canada and South Africa. After the Global Financial Crisis (GFC), the UK restructured its regulatory framework by replacing the integrated model with Twin Peaks model by bifurcating FSA in two institutions - the Financial Conduct Authority which focuses on market conduct, and the Prudential Regulation Authority (under the aegis of Central Bank) responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. The Twin Peaks model leverages potential synergies arising in the prudential or the business conduct oversight of various types of financial institutions but faces similar challenges of lack of sectoral focus as in the integrated model and co-ordination challenges as in sectoral model.

12. The **Two Agency** model is another example of the partially integrated model where one agency is responsible for the regulation and supervision of both solvency and conduct of business for banks and insurance companies, and a second agency is responsible for market integrity and the securities business. It is currently in place in jurisdictions such as France, Italy, Malaysia, Saudi Arabia, etc.

13. The models in the United States (US) and the European Union (EU) have special characteristics. While in the US functions have been assigned to various agencies at the federal and state level, in the EU, countries within the euro zone share a single prudential supervisory authority for significant banks. More recently, after the GFC, the macroprudential policy and resolution functions were the areas which were added to the financial oversight architecture, which may or may not involve separate agencies depending on the type of model adopted.

14. Each model includes trade-offs between synergies and potential conflicts of interest and challenges. The decision to adopt a financial oversight model depends on the structure and evolution of the financial sector, legal, cultural, and political economy considerations as well as past experiences like dealing with financial crises. Whichever be the model, one of the key features of any financial oversight architecture is the Central Bank remains the primary or lead authority. Its leadership in coordinating with other regulatory entities reinforces the coherence, resilience, and credibility of the overall financial oversight architecture.

15. Let me now touch upon the approaches adopted by regulators for the regulation-making process. While there may be differing views on the most apt approach to regulations, there is no ‘one size fit all’ approach. Regulators use different approaches and tools to address varied types of problems for effective regulation.

Principle vs. Rule vs. Outcome based regulation

16. Principle based regulation is qualitative and uses high-level statements with an explanation of the underlying intent. It gives flexibility and freedom to a Regulated Entity (RE) to innovate by developing new products and services without being constrained by prescriptive rules. However, it is open to subjective interpretation and can therefore pose challenges for both REs and supervisors, thus limiting enforcement

and accountability. It may also be less effective in areas like consumer protection, where clear and actionable directions are essential. In the context of Reserve Bank as a banking regulator, the Prudential Framework for Resolution of Stressed Assets[9] is an example of principle-based regulation.

17. Rule-based regulation, on the other hand, requires an RE to comply with specific, prescriptive requirements. It leads to better clarity, compliance, and consistency, as it simplifies the understanding of regulations for an RE and consumer alike. However, it may lead to a 'check-the-box' mentality, resulting in compliance by REs in letter but not in spirit. The REs may also face challenges when dealing with complex and dynamic issues where nuanced judgment is required. The Master Directions on Priority Sector Lending – Targets and Classification[10] can be considered as an example of a rule-based regulation issued by the Bank.

18. Another approach which has gained prominence of late is the outcome-based regulation, with focus on desired outcomes or results rather than prescribing specific processes and tools. This approach sets "what" is the desired outcome, while providing flexibility on "how" to achieve it. The RBI's Directions on Digital Lending[11] emphasise on the desired outcome, i.e., transparency and fairness for borrowers, rather than getting into specifics like lending rates or methods.

19. Striking the right balance amongst these approaches is critical to creating an enabling, and effective regulatory environment while encouraging innovation, given the complexities of today's dynamic financial landscape.

Activity vs. Entity based regulation

20. Activity-based regulation prescribes regulatory obligations for specific activities, independent of the entity undertaking them. It works on the principle of "same activity, same risk, same rules". The Directions issued on Financial Services provided by Banks[12] can be categorised as activity-based regulation.

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[9] https://rbi.org.in/web/rbi/-/notifications/prudential-framework-for-resolution-of-stressed-assets-11580

[10] https://rbi.org.in/web/rbi/-/notifications/master-directions-reserve-bank-of-india-priority-sector-lending-targets-and-classification-directions-2025

[11] https://rbi.org.in/web/rbi/-/notifications/reserve-bank-of-india-digital-lending-directions-2025

[12] https://rbi.org.in/web/rbi/-/notifications/master-direction-reserve-bank-of-india-financial-services-provided-by-banks-directions-2016-updated-as-on-august-10-2021-10425

21. In contrast, entity-based regulation aims to bolster the resilience of activities with focus on the entity. This approach encompasses governance, prudential and conduct requirements, reinforced by supervisory interventions. Given that an entity's overall resilience is shaped by the composition of its activities, entity-based regulations place targeted restrictions – an essential feature of such regulation. The prudential norms on capital adequacy are in nature of entity-based regulation.

22. Given the distinct regulatory domains, and keeping in view the objective of financial stability, regulators often adopt a hybrid approach that integrates elements of both activity-based and entity-based regulation. Such a tailored regulatory framework enhances the comprehensiveness and resilience of oversight mechanisms. It allows regulators to respond more effectively to market developments and emerging risks, thereby strengthening the overall regulatory architecture and promoting a sound, stable, and inclusive financial system.[13]

Rules based vs. Risk based approach[14]

23. Rules-based regulation focusses on adherence to regulatory prescriptions regardless of the level of risk. Though beneficial at times, the approach should factor in principle of proportionality, as not all entities carry same amount of risk to financial stability or consumer protection.

24. Adopting a risk-based approach enables regulators to frame regulations that are both effective and proportionate in the dynamic financial environment of today. This also helps in directing scarce regulatory and supervisory resources in optimal manner while also fostering innovation and financial inclusion. The Scale Based Regulation issued by RBI for Non-Banking Finance Companies (NBFCs)[15] and revised regulatory framework for Urban Co-operative Banks (UCBs)[16], can be thought of as recent examples of a risk-based approach.

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[13] https://www.fsb.org/uploads/P160724-2.pdf and https://www.bis.org/fsi/fsipapers19.pdf

[14] https://www.fsb.org/uploads/P160724-2.pdf

[15] https://rbi.org.in/web/rbi/-/notifications/master-direction-reserve-bank-of-india-non-banking-financial-copany-scale-based-regulation-directions-2023

[16] https://rbi.org.in/web/rbi/-/notifications/revised-regulatory-framework-categorization-of-urban-co-operative-banks-ucbs-for-regulatory-purposes-12416

Market vs. entity regulation

25. Market-based regulation focuses on the overall structure and functioning of financial markets, while entity-based regulation deals with the prudential norms, conduct, solvency, and internal risk management of individual financial institutions. Although each Financial Sector Regulator (FSR) such as the RBI, SEBI, IRDAI, PFRDA, or IFSCA has its distinct regulatory domain, activities of many of their REs overlap. Depending on their activities, these entities may fall under multiple regulatory frameworks, resulting in differential oversight and heightened operational complexity. For example, a mutual fund or an insurance company participating in government securities market or a bank participating in corporate bond market. To address such overlaps, FSRs are increasingly adopting a co-ordinated approach to regulation and supervision, with the broader goal of ensuring financial stability.

Challenges in regulation making

26. Regulation making is a complex process starting from identification of risks or gaps in existing regulations, evaluation of options to address them and finally coming out with an appropriate and effective regulation which is intended to address the risks for the entity and for the financial system (prudence, resilience and stability) and/or empower the consumers and ensure fair conduct amongst entities (conduct issues). While treading this path, the regulators are often confronted with many challenges. Let me highlight a few of them.

Balancing innovation and stability[17]

27. Innovation in the financial sector has brought about transformative changes. However, the rapid pace of innovation, also leads to regulatory gaps or grey areas. Innovations often take shape of new business models and partnerships with third parties, who are outside the regulatory ambit of the FSRs. It is the job of the regulator to plug these loopholes by framing rules in such a manner that allows innovation to thrive but provide sufficient guardrails to ensure that financial system remains stable and resilient. The regulators are therefore adopting a more agile and forward-looking approach - like the development of regulatory sandboxes and enhancing dialogue with

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[17] https://rbi.org.in/web/rbi/-/speeches-interview/financial-stability-in-the-emerging-technology-landscape

key stakeholders for integrating the new players into the regulatory framework, while being mindful of financial stability.

Keeping pace with emerging risks and technologies

28. The regulators need to keep pace with dynamically changing markets and deal with emerging risks and technologies. This requires regulators to devise approaches to ensure that consumers are treated fairly and also ensuring the safety of the financial system, while providing space for innovation. I would like to highlight two examples of the challenges faced by the regulators.

(I) **Climate risk**

29. Addressing climate change not only requires transition towards sustainability, but also integration of climate related financial risks into regulatory framework. Regulators across the world are debating whether climate risk warrants a separate framework or should it be embedded within existing risk categories. There is also ongoing discussion on whether climate risk oversight should form part of Pillar 2 (supervisory review), or Pillar 1 (capital and liquidity requirements). This continues to engage the attention of the standard setting bodies, industry and other stakeholders and there is a need to strike right balance to harmonize environmental stewardship with maintenance of financial stability.[18]

(II) **Emerging technologies**

30. New technologies improve ease of doing business, reduce operational and compliance costs, but they also pose challenges for regulation. There are three primary challenges in regulating these technologies: (i) the unpredictable nature of business models that rely on emerging technologies, (ii) data privacy, security, ownership, and control, and (iii) the artificial intelligence (AI) conundrum.[19] One example of new business models is Banking-as-a-Service (BaaS) model which increases scale and speed of distribution of financial products but could also lead to significant business conduct risks. Regulators face a dilemma: whether to come out with a framework before such financial innovations happen or allow markets to develop, risking unanticipated systemic risks and exploitative consumer practices.[20]

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[18] https://www.bis.org/review/r231115f.pdf

[19] https://digitalregulation.org/3004297-2/

[20] https://www.bis.org/review/r231115f.pdf

Additionally, regulators must navigate capacity constraints and legal complexities in crafting effective regulations.

31. Here too, we have adopted a cautious approach while coming out with regulations like digital lending directions covering partnerships between FinTechs (as Lending Service Providers) and REs, introduction of Video based Customer Identification Process (V-CIP) etc., in these emerging technology areas. The RBI had constituted a committee to develop a robust, comprehensive, and adaptable Framework for Responsible and Ethical Enablement of Artificial Intelligence (FREE-AI) for the Financial Sector[21] which has come out with a principle-based approach to AI adoption in the financial sector.

Reducing regulatory burden and ensuring compliance

32. India has made notable progress in improving its business environment over the years, however, there is still ample scope for further improvement. Regulatory burden and compliance costs pose challenges to REs, more so for smaller REs. Regulators not only need to do a delicate balancing act of reducing the burden and compliance cost for the REs but also need to ensure that it does not hinder the efficient functioning of markets. The Reserve Bank has pioneered some initiatives over time, which I would like to highlight:

a) To reduce compliance burden, RBI had constituted a Regulatory Review Authority (RRA) in 1999, followed by establishment of the second RRA (RRA 2.0) in 2021. The RRA 2.0 led to withdrawal or repeal of a total of 1,673 circulars, and discontinuation/ online conversion/ merger of 78 returns.
b) The ‘Connect 2 Regulate’ Platform has been introduced on RBI’s website to broaden involvement of members of the public and stakeholders in policy formulation and review, thereby making the process more consultative.
c) The ‘PRAVAAH’ (Platform for Regulatory Application, VAlidation and AutHorisation), a secure and centralised web-based portal for any individual or entity to seek authorisation, license or regulatory approval on any reference made to the Reserve Bank has been launched to enhance the efficiency of processes related to granting of regulatory approvals.

[21] https://rbi.org.in/web/rbi/-/publications/reports/free-ai-committee-report-framework-for-responsible-and-ethical-enablement-of-artificial-intelligence

d) To formalise participatory and responsive regulation making and demonstrating RBI's commitment to enhanced transparency and consultative approach a comprehensive Framework for the Formulation of Regulations was issued on May 7, 2025[22]. It lays down broad principles for drafting, amending, and reviewing regulations by the Reserve Bank.

e) The Reserve Bank is in the process of setting up a Regulatory Review Cell that would review all regulations every five to seven years.

Data, capacity and resource constraints

33. Another area which continues to engage the attention of the regulators is the lack of precise data to effectively formulate new policies. Rapid evolution of financial technologies has led to an exponential increase in the volume of data generated, however, challenges remain with respect to comprehensiveness, credibility, and accuracy of such information. Though regulators are equipping themselves with the latest tools and skills, the pace at which requirements are evolving is breath-taking. This requires continued capacity building within the regulators.

Inter-Regulatory co-ordination

34. As alluded to earlier, the Indian financial sector is characterised by significant heterogeneity, comprising of varied players governed by multiple FSRs, each responsible for entities operating under its purview. This demands robust and effective inter-regulatory co-ordination to facilitate consistent policy making. To address this challenge, an integrated approach to oversight has been adopted by the Financial Sector Regulators (FSRs) for financial conglomerates operating across multiple sectors, based on the 'lead regulator' principle. Joint supervision and periodic bilateral/multilateral discussions with such financial conglomerates are some of the tools adopted as a part of this approach.

35. The Financial Stability and Development Council (FSDC) headed by the Finance Minister and its Sub-Committee, headed by RBI Governor, where all heads of FSRs are represented, provides a platform for combined assessment of risks from the financial stability perspective and plays a pivotal role, for inter-regulatory co-ordination

[22] The key processes include (a) public consultation through issuance of a draft and a statement of particulars highlighting inter-alia the objective of the regulation, (b) impact analysis (to the extent feasible), (c) issuance of general statement of response to the public comments received, and (d) periodic review keeping in view aspects such as the stated objectives, experience gained, relevance in a changed environment, and the scope for reducing redundancies.

on the matters where there is overlap among FSRs. Such platforms help in further strengthening inter-regulatory co-ordination for wider development of financial sector in India.

36. However, there could be certain areas, such as increasing partnerships between the technological firms and the REs, where activities may fall outside the remit of any of the FSRs, exposing the REs to risks arising out of these activities. Addressing such risks, many a times becomes challenging for regulators and requires effective co-ordination among international regulators/ supervisors so that they do not lead to a systemic crisis. This remains a complex area for regulators, given the concerns around privacy, confidentiality, and enforcement.

Way forward

Principle and outcome-based approach

37. There is no perfect regulatory approach, however, principle and outcome-based regulation is generally found to be more suitable for mature markets. Nevertheless, even developed economies use rule-based framework when it comes to safeguarding interests of consumers. We, at the Reserve Bank are gradually shifting towards principle and outcome-based regulations, as it gives operational flexibility to the REs for conduct of their operations and tailor their activities to their unique needs, while adhering to the regulatory framework for delivering the outcomes expected from them.

Forward looking and proactive approach

38. Regulators are often confronted with complex challenges while framing regulations, necessitating adoption of a forward-looking approach. Addressing emerging risks calls for nuanced and adaptive strategies to ensure resilience. Regulators must adopt a more proactive mindset to help build a financial system that is both resilient and adaptable. Being proactive entails embracing innovation and fully leveraging data and technology. They need to further leverage technology to enhance their efficiency - both internal and supervisory, carry out regulatory horizon risk scanning and boost regulatory effectiveness. Usage of rapidly evolving technologies and collaboration with domain experts is need of the hour for the regulators to stay abreast of the evolving changes in the financial system.

Regulatory Impact Assessments (RIAs)

39. Regulatory Impact Assessments (RIA) are increasingly being recognised as essential tools for policy makers, enabling the development of policies that are grounded in evidence, clear in their purpose, proportionate in design, and responsive to real world conditions. These tools can be useful to strike a balance, by guarding against both unnecessary compliance burden and regulatory gaps, while boosting public confidence and enhancing international standing. Two essential elements of RIA are (i) Cost Benefit Analysis of the regulations, which can be evaluated either through qualitative or quantitative parameters or through a mix of both and (ii) consultation with a broad spectrum of stakeholders. While the latter leads to enhanced transparency, fostering trust, and improvement in the quality and effectiveness of the regulations, the former helps determine the optimal solution for addressing the problem while ensuring efficient allocation of resources.

40. Another important area is timely review of regulatory prescriptions and reporting mechanisms with a view to streamlining/ rationalising them and making them more effective. Such timely reviews not only reduce compliance requirements but also offer the regulators an opportunity to review the appropriateness of regulations in line with evolving market practices and developments. Regulators should endeavour to adopt best practices in their regulatory approaches, both ex-ante, to assess potential impact and avoid unintended consequences and ex-post, to assess actual impact and support course correction while enhancing future rule design, so that together, they ensure that regulation is both “right the first time” and “kept right over time”.

Enhancing compliance

41. The regulators should have a broader vision of enhancing compliance by REs to make it easier for them to comply with regulations. This can be done by simplifying regulations, enhancing their clarity and removing redundancies and duplications. The Reserve Bank has been emphasising on clarity in regulations and has started including examples, FAQs and illustrations as a part of its regulations for the benefit of the REs. To provide a high-level overview of the regulatory landscape and serve as a broad point of reference for general understanding of the REs, the Reserve Bank

had come out with a Handbook titled ‘Regulations at a Glance’[23]. Further, the Reserve Bank is in the process of consolidating more than 8,000 regulations issued by Department of Regulation, under 30-35 thematic subjects. The regulators need to persist with such initiatives for enhancing the responsiveness of the REs and development of the financial sector.

International and domestic regulatory co-operation

42. Given the cross sectoral operations of entities, there is a need for the FSRs to move away from siloed, sector-specific regulations towards cross-functional principle-based regulations. This co-ordination will foster innovation and enable the REs to offer services across different domains as also ensure that they have appropriate risk management protocols. This would also help in capping regulatory arbitrage, while simultaneously reducing compliance requirements for the REs. Additionally, co-operation among regulators across jurisdictions is essential for sharing insights, expertise, and resources to enable more efficient regulation without compromising on quality.[24] International standards serve as a valuable reference point; however, they must be adapted to local contexts and conditions, as a 'one size fits all' approach is neither practical nor effective in today’s diverse regulatory landscape.

Consumer centricity

43. We need to consider the impact that regulations can have on one of the most important stakeholders in financial system i.e., consumers. Regulators have remained conscious of the need to empower consumers and safeguard their interests. To advance this objective, they must think beyond conventional approaches. Behavioral economics offers a powerful tool in this regard, providing valuable insights into consumer behavior and decision-making processes. It equips the regulators with an advanced set of policy instruments, most notably, behavioral nudges[25], which can complement conventional regulatory frameworks by achieving the desired outcomes at far lower compliance costs, thus presenting a more efficient and socially beneficial policy alternative.[26]

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[23] https://rbi.org.in/web/rbi/-/press-releases/release-of-handbook-on-regulations-at-a-glance-

[24] International Regulatory Co-operation – Policy Brief by OECD April 2020

[25] According to Thaler and Sunstein (2008, p. 6), a nudge is any aspect of the choice architecture that alters people’s behavior in a predictable way without forbidding any options or significantly changing their economic incentives. To count as a mere nudge, the intervention must be easy and cheap to avoid. Nudges are not mandates.

[26] https://behaviouraleconomics.pmc.gov.au/blog/more-nudges-value-behavioural-economics-regulation

Conclusion

44. Regulatory policy in the financial sector must strike an optimal balance between the critical need for stability and objectives of fostering innovation, efficiency, and competition. While it is necessary to minimise systemic risks and protect consumers, it should not discourage creativity, innovation, or healthy market dynamics. On the other hand, an overemphasis on innovation and competition - without adequate safeguards - can lead to financial instability, resource misallocation, and ultimately loss of confidence in the system. Finding this right balance is particularly important for India, given the immense size and heterogeneity of economy, growing aspirations, and substantial investment needs to sustain high growth and development. The regulators must consistently strive to achieve this equilibrium. As Mahatma Gandhi said, "*You may never know what results come of your actions, but if you do nothing, there will be no result*."

Thank you once again for the opportunity to share my thoughts with you. I wish all participants an enriching and successful deliberations in the programme.