The financial sector in India

- The regulators
  RBI, SEBI, FMC, IRDA, PFRDA, MoF, HLCC

- The markets
  Commodities, equity, debt, foreign exchange

- The players
  Brokers, firms, banks, financial institutions, foreign institutional investors, mutual fund managers, investors, exchanges, depositories, custodians, registrars.
RBI

- Set up under the RBI Act, 1935.
- Regulator of deposit-taking agencies.
- Regulator for debt, foreign exchange markets.
- Securities infrastructure for debt, foreign exchange markets.
- Payments system.
- Investment banker for the government.
- Central bank.
FMC

- Flows from the FC(R) Act 1952.
- Regulator of commodity derivative markets, commodity derivative brokers.
- FMC regulation is in the form of policy recommendation rather than implementation (which is done by the DCA) or enforcement/punitive action (which is done by the police).
- Plays a role in the development of commodity derivative markets.
- Is an arm of Department of Consumer Affairs.
SEBI

- Set up in 1988, as part of the SC(R) Act 1956.
- The first regulator under the SC(R)A, 1956 was the CCI.
- Regulator of anything that is exchange-traded.
- SEBI can set regulatory policy, carry out implementation as well as has the power to enforce regulatory rules and impose punishment on wrong-doing.
- Grievances and appeals to SEBI rulings are heard by the Securities Appellate Tribunal.
MoF

- Plays a role in creating regulators.
- Prior to the reforms of the nineties, played the role of supervisor of rules and regulations.
- Legislative work.
- Big picture policy questions that go beyond the agenda of any one regulator.
- Conflict of interest: owner of many finance companies.
Co-ordination between regulators.

Members:
- Governor, RBI
- Chairman, SEBI
- Chairman, IRDA
- Finance Secretary, MoF

Member secretary: Joint Secretary, capital markets, at MoF.
Problems with the current regulatory structure
Difficulties

- Failure to exploit economies of scale. Example: Commodity futures trading could not take off at NSE/BSE.
- Turf conflicts.
- Inhibits products and markets when they involve multiple regulators.
SBI, ICICI, HDFC: These may be many distinct firms, but they are really one big conglomerate. They are “virtual firms”.

Conglomerates are given an edge in the current regulatory architecture.

No one regulator knows the full picture.

TBTF issues.
Goals of regulation
De facto “principles of regulation”

1. Price stability.
2. Protecting the small investor.
3. Preventing market misconduct.

Do these goals lead regulators into the right behaviour?
The effect of good regulation ought to mean better market outcomes.
Example: FSA’s principles statement

1. Using resources in the most efficient way.
2. Be “proportionate” in imposing burden on industry.
3. Facilitate innovation.
4. Think globalisation.
5. Do not impede or distort competition.
What can architecture reforms achieve?

- It is important to distinguish problems of architecture from problems of implementation.
- HR problems; process problems: these will remain under any architecture.
Alternatives
I. Integrated regulation

- UK, Japan, Korea, etc. have gone this path.
II. Rajan & Shah proposal

- Create a separate regulator for the 10 large conglomerates.
- That separate regulator should have one-stop approval power for all innovations that go beyond one regulator.
III. Incremental work within present system

- Take stock of all the regulators, their legal framework,
- Incrementally make improvements, remove decades-old design decisions, clarify mandate.
- This does involve opening up questions about mandate.
- Need better harmonisation of principles of regulation across the various regulators.