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**Balancing Prudential Regulation and Competition Considerations in Banking –
Background Note**

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Balancing prudential regulation and competition considerations in banking

This paper examines the possible tensions, trade-offs, and complementarities between prudential regulation and competition in banking. Well-calibrated prudential rules, along with effective competition policy and enforcement, can jointly foster financial resilience, efficiency and innovation. Focusing on retail deposits and lending, the paper examines how competition and prudential regulations may strike a balance between stability and open and dynamic markets. It highlights considerations in aligning prudential and competition objectives through proportionate, risk-based regulation. It also stresses the need for sustained co-operation between prudential and competition authorities to ensure these core banking markets deliver lasting benefits for consumers and the economy.

Keywords: competition in banking, prudential regulation, competition and innovation, competition policy, regulatory effectiveness

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Executive summary

Sound retail banking markets drive productivity and growth, and prudential regulation ensures resilience and stability by mitigating systemic vulnerabilities and maintaining trust in the banking system.

Well-functioning retail banking markets are critical to supporting economic productivity, long-term growth, economic resilience and financial stability.¹ Banks hold a significant share of household wealth and create commercial money by extending vital credit to households and businesses.² Yet these same functions generate vulnerabilities, such as liquidity mismatches, interbank linkages and information asymmetries.³ Prudential regulation governs financial activities and imposes licensing requirements and minimum capital standards to mitigate these vulnerabilities and maintain depositor confidence. By screening entrants and ensuring that banks hold sufficient buffers to absorb losses, it aims to reduce the likelihood of institutional failure, limit systemic contagion and safeguard the financial system.

Competition in banking, in turn, is a key driver of efficiency, innovation and improved consumer outcomes.

Dynamic, contestable markets lower borrowing costs, improve deposit conditions, and expand both the quality and diversity of financial services. By ensuring that entry remains feasible and exit credible, contestability keeps pressure on incumbents, disciplines market power, and channels resources toward productivity and improved consumer outcomes. Competition can also reinforce resilience by fostering higher-quality institutions, which, alongside effective prudential oversight, can help to curb excessive risk-taking.

Nevertheless, there are some inherent tensions between prudential and competition policy goals.

Where contestability relies on the possibility of entry and exit, prudential regulation seeks to prevent disorderly exits that may trigger runs or contagion.⁴ Prudential tools to safeguard stability may, at times, inadvertently raise barriers to entry and expansion, entrench incumbents or slow innovation. Conversely, limited prudential supervision of new entrants, such as non-bank financial intermediaries (NBFIs), including FinTechs and BigTechs, which are increasingly performing bank-like functions, may pose prudential risks.⁵

Effective prudential regulation, like other public policies, benefits from balancing trade-offs across different time horizons, including effects on competition.

All prudential rules shape market dynamics, for example, by limiting entry into certain financial activities or setting capital requirements. Prudential safeguards can be designed to take competition into account. This may involve ensuring that rules minimise bottlenecks to competition, are competition-neutral, or facilitate competition. Balancing competition and prudential goals takes on greater significance amid opportunities arising from digitisation and new entry, as well as the emerging risks they pose, including through bank-NBFI interdependencies. Trends toward consolidation in retail deposits and lending services may heighten tensions over policy remits and give rise to shared concerns about market power and potential systemic risks.⁶ While regulatory frameworks differ across countries, as do market structures and the role of NBFIs, the challenge of reconciling prudential and competition goals is widely shared.

Policymakers, prudential regulators and competition authorities have an essential role to play in managing trade-offs and supporting the sector's adjustment to challenges.

Prudential regulation and competition policy can be complementary and, at times, reinforce one another. Through effective co-operation and a balanced pursuit of their respective objectives, banking markets can become more resilient, efficient and innovative, delivering lasting benefits for consumers and the wider economy. To inform this balancing, this paper examines core banking services (retail deposits and lending) by both

banks and NBFIs. It builds on prior OECD work, including discussions on prudential regulation and competition in financial markets (2009^[1]), bank competition and financial stability (2011^[2]), and co-operation between competition agencies and regulators in the financial sector (2017^[3]).

The paper highlights several considerations regarding the interaction between prudential regulation and competition policy:

- **Prudential and competition objectives can interact in complex ways.** The two policy areas are sometimes complementary, but at other times may pull in different directions. Understanding and managing these dynamics can be important to avoid long-term distortions in core banking markets.
- **Digitisation and new entry broaden both opportunities and risks.** The growing participation of FinTechs, BigTechs and other NBFIs introduces new forms of competition and innovation, but also new challenges and interdependencies relevant to both policy remits.
- **Prudential rules inevitably shape market structure and competition.** Licensing and capital requirements play a central role in safeguarding stability, but if not well-calibrated, they may unnecessarily limit entry, expansion, or exit and reinforce incumbency.
- **Credible exit frameworks can mitigate risks.** Mechanisms that allow inefficient financial institutions to exit the market in an orderly way can mitigate systemic risk and reduce long-term distortions to competition.
- **Proportionate, risk-based frameworks may help reconcile objectives.** Calibrating prudential requirements proportionally to size, complexity or risk profiles can preserve contestability while maintaining stability.
- **Competition policy and enforcement can support prudential outcomes.** By preventing exclusionary or co-ordinated practices and anticompetitive mergers, competition enforcement can contribute to more resilient and efficient markets.
- **Effective regulatory co-operation enhances policy coherence.** Regular dialogue and co-ordination between prudential and competition authorities can help ensure that measures designed to protect stability also sustain, or do not unnecessarily limit, the benefits of competition.

1 Background and analytical foundations

1.1. The objectives of prudential regulation

1. Banking markets are especially vulnerable to instability, particularly from asset-liability mismatches. A core retail banking function is to collect deposits and extend loans, with deposits complementary to loan provision (Vives, 2016^[4]). Banks act as intermediaries between lenders and borrowers, creating liquidity but also exposing themselves to two persistent challenges: (i) co-ordination failures that can trigger liquidity mismatches, as short-term savings are pooled to finance long-term credit and (ii) asymmetric information between banks and borrowers, which makes it difficult to assess the risk and quality of loans, increasing the likelihood of non-performing assets and sudden losses of confidence. These frictions expose banks to solvency pressures, liquidity shortfalls and depositor runs (Carletti and Hartmann, 2002^[5]).⁷

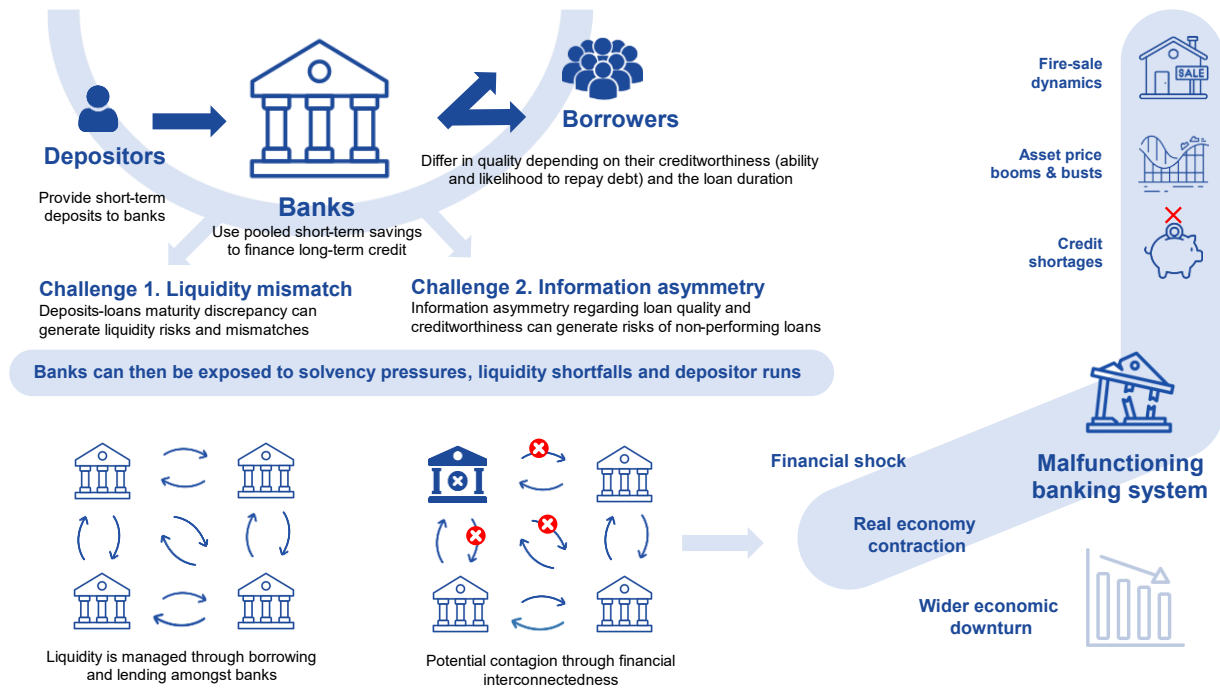
2. Banks also borrow and lend extensively among themselves to manage liquidity. This interconnectedness means the distress of one bank can transmit shocks across the system, propagating contagion (Carletti and Hartmann, 2002^[5]). Risky lending or default by one bank can cascade across counterparties, amplifying systemic effects. When households and firms lose access to deposits or credit, the contraction in spending and investment can rapidly spill over to the wider economy (OECD, 2017^[3]). A malfunctioning banking system can generate significant negative externalities for the broader economy, including credit shortages, fire-sale dynamics due to asset-liability mismatches, asset price booms and busts, and feedback loops between banks and sovereign debt markets that can amplify both financial and fiscal fragilities (Stein, 2012^[6]; Brunnermeier et al., 2016^[7]). Figure 1 below provides a visual representation.

3. To mitigate these systemic risks, prudential regulation has been adopted across jurisdictions (Vives, 2016^[4]; Hohl et al., 2018^[8]). Prudential regulation seeks to safeguard the stability and soundness of the financial system. It is designed to make deposit-taking and lending institutions more resilient to shocks, reduce the risk of failure and maintain confidence among depositors, borrowers and counterparties. By doing so, it helps ensure that credit provision and savings intermediation continue even in periods of stress (OECD, 2011^[2]). Prudential regulation takes two complementary forms: micro-prudential and macro-prudential rules, which differ in scope and instruments but share the goal of resilience.

- **Micro-prudential regulation** focuses on the resilience of individual banks. It seeks to prevent failures that could directly endanger depositors and undermine confidence. This is especially important in deposit and lending markets, where the collapse of one provider can disrupt consumer savings and credit supply (Boissay and Cappelletto, 2014^[9]).⁸
- **Macro-prudential regulation** addresses system-wide stability by monitoring and mitigating risks across the banking sector rather than at the level of a single firm.⁹

4. Micro-prudential and macro-prudential regulation are complementary and increasingly interconnected tools in preserving stability.¹⁰ This note focuses primarily on (i) micro-prudential measures, such as licensing and capital requirements, which have direct influence on market entry, cost structures and the competitive dynamics of deposit and lending markets and (ii) macro-prudential frameworks, such as resolution regimes, implemented through micro-prudential tools, which aim to mitigate systemic risk and contain the broader impact of institutional failure (OECD, 2017^[10]; White, 2014^[11]; Ahrend, Arnold and Murtin, 2009^[1]; González, 2022^[12]).

Figure 1. Banking market stability: challenges and vulnerabilities



Source: OECD.

1.2. The relationship between prudential regulation and competition policy

1.2.1. Complementarities between prudential regulation and competition policy

5. Competition in the banking sector can fuel efficiency, quality and innovation. It determines how widely and affordably households and firms can access deposits and credit: services that underpin investment, consumption and long-term growth for the economy (OECD, 2011^[2]; de Serres et al., 2006^[13]). Where competition is weak, consumers face higher prices, lower quality and fewer choices (OECD, 2011^[2]). Prudential regulation and competition policy can be complementary, but they are not substitutes; each achieves outcomes that the other cannot (Vives, 2025^[14]). When pursued together and balanced, they can reinforce productivity and resilience. The following discussion, though not exhaustive, highlights certain complementarities.

6. First, historically intense competition was perceived as a potential risk factor for stability (Vives, 2016^[4]). The concern was that excessive competition could erode margins, reduce franchise value and lead banks to take on excessive risk, undermining depositor trust and sparking runs. It was also thought to worsen co-ordination problems and increase systemic risk (Cœuré, 2025^[15]). For decades, these

concerns shaped regulatory approaches, leading to exemptions, limited enforcement, or sector-specific regimes that constrained the application of competition law in banking.

7. However, evidence suggests that competition can support stability when coupled with appropriate prudential safeguards (Vives, 2016^[4]). For example, Schaeck et al. (2009^[16]) show, using data from forty-five countries, that competition reduces the likelihood of a crisis and that the time between crises is longer in a more competitive environment. Other studies confirm that competition can enhance systemic stability and that a more competitive market can go hand in hand with a lower level of bank risk (Shehzad and de Haan, 2009^[17]; Anginer et al., 2019^[18]; Kick and Prieto, 2013^[19]). Additional studies conclude that competition in the loan market may reduce risks in banks' portfolios by influencing borrowers' risk-taking behaviour (OECD, 2017^[3]).¹¹ For borrowers, less competition in banking means higher loan rates, lower profits and increased risk-seeking behaviour. Evidence shows that, as a result, increased competition in loan markets can lower the risk of bank failure by reducing borrowers' default risk. Studies also examine how competition may increase the cost of bankruptcy and thus act as a disincentive to risk-taking (OECD, 2017^[3]; Boyd and De Nicolo, 2003^[20]). Generally, empirical and policy evidence suggest that competitive banking markets can support efficiency and strengthen financial stability (OECD, 2011^[2]; Vives, 2016^[4]; BCA, 2023^[21]).

8. Well-calibrated prudential rules can reinforce the benefits of competition by promoting contestability and enabling exit, while preserving resilience in deposit and lending markets. This shift in perception reflects cross-country research and post-crisis reforms showing that competition and stability can be complementary (OECD, 2017^[3]; Vives, 2016^[4]). It also underscores the recognition that a lack of competition can pose prudential risks, for example, by entrenching institutions whose failure would have severe systemic consequences (Inderst, 2013^[22]). Competition enforcement can thus play a crucial role in strengthening prudential objectives by ensuring a level playing field, preventing anticompetitive effects from materialising.

9. Second, competition can help amplify the effectiveness of prudential regulation and vice versa. Competition can fuel better-quality institutions, improve monitoring and reporting incentives and reduce the scope for excessive risk-taking (OECD, 2017^[3]). That is, competition improves the monitoring incentives of better-quality banks (Carletti and Vives, 2008^[23]). When banks differ in the underlying riskiness of their operations, stronger competition tends to discourage additional risk-taking by already prudent institutions (Inderst, 2013^[22]).¹² Prudential rules that enforce sound risk management and reporting obligations enable well-managed banks and reduce information asymmetries for depositors. Well-regulated markets build trust, which in turn enables competition. In this sense, competition provides a strong foundation for successful policy implementation.

10. Third, effective competition can help reduce the systemic importance of inefficient banks. The benefits of competitive pressure are manifold. Contestability and the threat of entry may not only discipline incumbents to manage risks more effectively but also spur efficiency and innovation. Diversity also reduces the reliance on a few systemically important firms. More contestable and less concentrated markets can ensure that the failure of one institution poses less systemic risk. In turn, large banks may tend to be more interdependent, increasing systemic risk (Laeven, Ratnovski and Tong, 2014^[24]). Higher concentration can be associated with greater potential for financial instability due to the cost of credit, diversification and the ease of monitoring (Calice and Leonida, 2018^[25]). Where the market is both concentrated and firms are interdependent or interconnected, acting as counterparties to each other, should one such firm fail, the financial viability of all of its counterparties is called into question (OECD, 2011^[26]).

11. Moreover, too-big-to-fail (TBTF) institutions face moral hazard or distorted incentives: they may take excessive risks, expecting bailouts or benefit from implicit guarantees that lower their funding costs. This can undermine both stability and competition. Prudential and competition authorities thus share an interest in addressing moral hazard and limiting TBTF distortions.¹³ While limiting moral hazard is typically

the role of prudential regulators, competition can help limit the emergence of TBTF institutions and, where they exist, subject them to competitive pressure, taming distorted incentives (OECD, 2017^[10]).

12. Fourth, competition can facilitate the exit of inefficient banks. Without it, weak institutions may persist, draining resources and increasing the risk of contagion. In turn, poorly designed prudential policies may inadvertently prop up failing institutions. As addressed in Section 3.1.2, post-crisis resolution regimes can be designed to facilitate a “safe” exit while minimising systemic fallout. This represents growing convergence between prudential and competition authorities: both recognise that shielding inefficient institutions may undermine stability and distort competition (Cœuré, 2025^[15]).

13. Fifth, competition and effective prudential oversight can encourage banks to take on more diversified risks, making the banking system less fragile to shocks (Anginer, Demirguc-Kunt and Zhu, 2014^[27]). Competition can reduce co-ordination risks that may undermine both market outcomes and prudential objectives. Such risks, like in other sectors, arise when relatively homogeneous products and concentrated market structures enable market participants to anticipate and align their behaviour. In deposit and lending markets, similar pricing frameworks and product designs enable banks to monitor rivals’ actions, even when consumers perceive offers as heterogeneous due to complex terms and conditions. This asymmetry: transparency among banks but opacity for consumers, weakens rivalry, facilitates co-ordination and harms both consumers and financial stability (BCA, 2023^[21]). Competitive pressure helps counteract these tendencies by fostering greater strategic differentiation, innovation and diversity of risk exposures.¹⁴ In this way, competition can support prudential objectives by reducing the likelihood that parallel decisions or common shocks translate into systemic fragility (Anginer and Demirguc-Kunt, 2014^[28]).

14. Section 3.2 highlights certain concrete examples of how competition policy and enforcement may advance stability objectives. For example, competition can help reduce interest rate spreads: the gap between what banks charge on loans and pay on deposits. Protecting rivalry between lenders can lower borrowing costs and help reduce borrower defaults, decreasing systemic risk (OECD, 2017^[3]). In sum, competition drives efficient financial intermediation, supporting growth and innovation across the wider economy (Siciliani et al., 2023^[29]).

15. Taken together, these complementarities illustrate that prudential regulation and competition policy, when designed with an awareness of their interaction, can be complementary. However, this alignment is not automatic. Measures that enhance stability may sometimes constrain rivalry and vice versa. The next section examines these areas of possible tension and the trade-offs they present for policymakers.

1.2.2. Tensions between the objectives of prudential regulation and competition

16. There are inherent tensions between prudential regulation and competition policy’s goals. These tensions and their related trade-offs span multiple dimensions (Vives, 2016^[4]). The following discussion is not exhaustive; it highlights certain tensions relevant to deposit and lending markets when balancing policy objectives. Importantly, the distinct mandates, time horizons, and risk tolerances of prudential and competition authorities can shape how each assesses the same market developments. Moreover, these frictions are not static: they may intensify in periods of stress or when reforms shift the boundaries of each policy’s remit. The degree of divergence varies across jurisdictions, depending on market structure, institutional frameworks and the nature of the institution concerned. Box 1 discusses how national financial market structures may shape the interaction between prudential regulation and competition policy.

Box 1. Financial market structures and their implications for competition

The relationship between prudential regulation and competition policy varies across jurisdictions, reflecting differences in financial market structure, institutional design and levels of financial development. For example, in many European economies, financial intermediation remains predominantly bank-based, whereas in the United States (US), capital markets play a larger role in financing firms and households. These structural differences may affect how competition in banking can impact credit availability and risk dispersion. In market-based systems, competition in securities and bond markets may, to some degree, provide alternatives to traditional lending.

Since the Glass-Steagall Act of 1933, the US has historically separated commercial and investment banking to limit the transmission of risk. This boundary blurred under the Gramm-Leach–Bliley Act of 1999, which allowed financial holding companies to engage in both activities under prudential supervision. While the institutional separation has not been reinstated, post-Global Financial Crisis reforms, such as the Volcker Rule, have introduced a form of functional separation by limiting proprietary trading and certain investment activities. In contrast, many European banks operate as universal banks, combining deposit-taking and investment activities under a single balance sheet, creating both potential efficiencies and potential channels for contagion.

In emerging economies with lower banking penetration, non-bank financial institutions (NBFIs), including FinTechs, BigTechs and mobile network operators, often play a key role in expanding access to credit and payments, sometimes leapfrogging the need for traditional banks.

From a competition perspective, these structural distinctions shape both the scope of rivalry and the potential for vertical or conglomerate effects. For instance, between deposit-taking, securities issuance and asset management. Consequently, while general principles of complementarity and trade-offs apply broadly, the balance between prudential and competition objectives will differ across financial systems, including based on the levels of market development.

Source: Langfield, S and Pagano, M (2016), Bank bias in Europe: effects on systemic risk and growth, <https://doi.org/10.1093/epolic/eiv019>; Neal, L. and White, E (2012), The Glass–Steagall Act in historical perspective, <https://doi.org/10.1016/j.qref.2011.12.005>; Board of Governors of the Federal Reserve System (2020), Volcker Rule, <https://www.federalreserve.gov/supervisionreg/volcker-rule.htm>; OECD (2025), Competition in mobile payment services, *OECD Roundtables on Competition Policy Papers*, No. 324, OECD Publishing, Paris, <https://doi.org/10.1787/0ce6b5d3-en>.

17. A first area of tension concerns contestability, which is central to effective competition in deposit and lending markets. The threat of entry (actual or potential) disciplines incumbents to innovate, offer better rates and higher quality. However, opening markets to new entrants can also magnify prudential risks if those entrants are not adequately supervised or capitalised.

18. This raises an “in-or-out” trade-off: prudential regulation often requires that any firm engaging in banking-like activities be “in” the supervisory perimeter before operating. Licensing requirements, including capital requirements, protect stability but may also raise entry and expansion barriers that may unintentionally dampen competition. Conversely, leaving providers outside the perimeter risks instability, particularly if they become large or interconnected enough to transmit shocks. In short, if firms are in, competition may suffer; if they are out, stability may be at risk (PRA, 2021_[30]). This dilemma is especially salient in fast-moving markets shaped by digitisation, where the boundary between “in” and “out” may shift rapidly as business models scale and interconnect, as discussed in Section 2. Because perimeter choices have lasting implications for both competition and systemic resilience, Section 3.1.1 briefly considers how to seek a potential balance.

19. Relatedly, the potential for exit can reallocate resources toward more efficient providers. Without it, weak business models may persist through regulatory forbearance or support measures, potentially

reducing efficiency and raising risks over time. Yet, in banking, a disorderly exit, such as the abrupt failure of a financial institution without adequate loss-absorption capacity or resolution planning, can trigger depositor runs, contagion and the interruption of critical functions such as lending, with spillover effects that extend across the economy. This creates a unique tension: while competition policy may view exit as a mechanism for efficiency, prudential authorities may see it as a source of instability (Cœuré, 2025^[15]). These differing perspectives can lead to divergent recommendations in supervision or enforcement, particularly during crises.

20. For example, during crises, prudential authorities may support mergers, state support or other interventions to preserve stability, even when these raise competition concerns (OECD, 2011^[26]; OECD, 2021^[31]). Past responses, including TBTF policies such as bailouts or state aid, often entrenched incumbents and distorted markets. Limiting liability also created moral hazard, encouraging excessive risk-taking under the assumption of a safety net. Such interventions, justified by short-term stability goals, can produce long-term distortions to competition that are costly to unwind. In recent years, however, the design of bank resolution regimes has evolved to reduce these tensions. As discussed in Section 3, effective resolution strategies now aim to balance financial stability and competition (Coeuré et al., 2024^[32]).

21. Second, another source of tension concerns financial innovation. While innovation is often associated with competitive benefits, economic evidence suggests an “inverted U” relationship between competition and innovation (Aghion et al., 2005^[33]). That is, when the degree of competition is low, greater rivalry tends to spur innovation, whereas beyond a certain point, further increases in competition may reduce incentives to innovate (OECD, 2023^[34]). Reviewing the empirical and theoretical literature, Griffith and Van Reenen (2021^[35]) conclude that, on average, the relationship between innovation and competition tends to be more positive than negative. From a competition perspective, this implies that in many markets, greater competition is needed to foster more innovation. In financial markets, however, historical experience shows that some forms of financial innovation, such as derivatives, have amplified instability and triggered crises (Aliber and Kindleberger, 2015^[36]). This underscores why prudential authorities may take a more cautious view of innovation than competition authorities.

22. Third, banks and NBFIs must remain profitable to build capital buffers and meet regulatory requirements, aligning prudential and competition goals when profits stem from efficiency. However, tensions may arise when profitability stems from anticompetitive conduct, leading to differing assessments by authorities, particularly when prudential stability considerations prevail in short-term decision-making. Moreover, while certain forms of co-operation, such as interoperable ATM networks, may be justified on prudential grounds and generate efficiency benefits, co-operation amongst rivals also carries the risk of collusion (Vives, 2016^[4]). In the past, some banking cartels were condoned by central banks or regulators in the interest of financial stability (OECD, 2008^[37]; 2011^[38]; Vives, 2016^[4]). Today, such practices are typically subject to standard competition enforcement, including leniency programmes and penalties (Vives, 2016^[4]). Importantly, the threat of large penalties and the reputational damage that accompany antitrust enforcement are important deterrents to financial market misconduct (Gandhi et al., 2019^[39]). Box 2 discusses the resulting distortions in competition and the delay in economic recovery from weakened cartel enforcement generally during past crises.

Box 2. The negative consequences of weakened cartel enforcement

Past experiences across jurisdictions demonstrate that, during times of crisis, generally relaxing competition enforcement against cartels, intended to promote stability, can lead to enduring distortions in competition and delay long-term economic recovery.

The United States

In the US, cartel enforcement weakened during the Great Depression. The National Industrial Recovery Act of 1933 introduced broad antitrust exemptions across industries and provisions aimed at stabilising prices and raising wages. Although the Act was declared unconstitutional in 1935, many of the co-operative arrangements it enabled continued to influence market behaviour despite subsequent anti-cartel enforcement. Empirical studies have since found that these policies contributed to the persistence and depth of the Great Depression. Research suggests that these measures reduced consumption and investment by roughly 14% relative to competitive levels between 1934 and 1939.

Japan

In Japan, policy measures introduced to counter recessions in the 1950s and 1960s included the establishment of “depression” or “rationalisation” cartels, which allowed firms to co-ordinate production, reduce capacity and, in some cases, align prices. These interventions were later recognised as having adverse medium and long-term effects on competition and were subsequently abolished.

Research suggests that the lax application of competition law prolonged the recession in the US during the 1930s. Similarly, research on Japan's economic downturn indicates that government intervention to restrict competition in structurally depressed industries prolonged the recession in the 1990s.

Source: OECD (2011), *Competition Issues in the Financial Sector: Key Findings*, OECD Publishing, Paris, <https://doi.org/10.1787/37dd5552-en>; Harada, K. and Ito, T. (2008), Did Mergers Help Japanese Mega-Banks Avoid Failure? Analysis of the Distance to Default of Banks, <https://www.nber.org/papers/w14518>; Independent Commission on Banking (2011), Final Report Recommendations, <https://webarchive.nationalarchives.gov.uk/ukgwa/20120827143059/http://bankingcommission.independent.gov.uk/>; Crane, Daniel A. (2008). "Antitrust Enforcement During National Crises: An Unhappy History" Global Competition Policy, December 2008, www.globalcompetitionpolicy.org; Porter, Michael E., Takeuchi Hirotaka and Mariko Sakakibara (2000). *Can Japan Compete?* Cambridge, Mass.: Perseus Publishing, London, Macmillan; OECD (2011), "Crisis Cartels : Key findings, summary and notes", OECD Roundtables on Competition Policy Papers, No. 119, OECD Publishing, Paris, <https://doi.org/10.1787/39a0d2e8-en>; Cole, H. and Ohanian, L (2004), *New Deal Policies and the Persistence of the Great Depression: A General Equilibrium Analysis*, <https://doi.org/10.1086/421169>.

23. Fourth, tensions can also stem from differences in how sectoral and competition authorities intervene in markets (Cœuré, 2025^[15]). Competition authorities typically act *ex post* (except in merger enforcement, which tends to be *ex ante*), addressing exclusionary anticompetitive conduct through targeted, one-off interventions. By contrast, sector regulators, particularly prudential supervisors, work *ex ante* and exercise continuous and discretionary oversight to prevent risks and sustain market confidence (Cœuré, 2025^[15]). Their forward-looking mandate reflects the high costs of banking instability and the potential need for preventive action. Prudential authorities can influence market structure not only through licensing conditions and merger approvals (which are often also under the purview of competition authorities across jurisdictions), as other sector regulators do, but also through their powers over resolution, recovery planning, and assessment of the ongoing viability of institutions, playing a continuous and systemic market-shaping role. As a result, prudential regulation may be perceived as shaping markets *ex ante*, whereas competition authorities typically act *ex post* to repair markets, in accordance with principles of liability (Vives, 2016^[4]). This difference may lead to prudential regulation being treated as a substitute rather than a complement to market forces or competition enforcement, highlighting the importance of co-ordination between prudential and competition authorities.

24. While trade-offs are inherent, prudential regulation and competition policy can be neutral or, at times, reinforce one another when designed in a complementary way. The challenge and opportunity for policymakers is not only to manage tensions but also to actively harness complementarities to ensure that deposit and lending markets remain resilient and dynamic. The remainder of this section outlines the deposit and lending services landscape as background to the discussion that follows.

1.3. Background to deposits and lending services

1.3.1. Structural barriers to entry and expansion

25. Switching costs and lock-in are persistent barriers to entry and expansion in retail deposit markets. Across jurisdictions, evidence of low consumer mobility in deposits has led to the adage that a consumer is more likely to divorce than to switch bank accounts. Low mobility persists even where there are sizable gaps between the initial offers on deposit interest rates and the rates most customers actually earn (ACCC, 2023^[40]; BCA, 2023^[21]; ComCom, 2024^[41]; FCA, 2023^[42]). Switching costs thus act as an important source of market power in retail banking (Carletti, Leonello and Marquez, 2024^[43]).

26. Consumers face persistent challenges in searching for and comparing offers, as well as in executing a switch.

- Information asymmetries fuel consumer lock-in. In deposits, heterogeneous products, bundling of accounts or services, and the divergence between initial or bonus offers and base rates make an apples-to-apples comparison difficult. That is, even seemingly comparable products can differ materially in terms and conditions, which increases confusion and reduces the salience of superior alternatives. This raises search costs and mutes the threat of consumer departure.
- Price design amplifies lock-in. Many banks rely on introductory or bonus rate structures that expire quickly while the base rate remains low. Once balances revert to low base rates as the default, most customers stay put due to inertia. This “reversion pricing,” where a product is offered at an attractive rate initially, and later automatically reverts to a lower rate, takes advantage of limited switching and rewards incumbents (ACCC, 2023^[40]).
- The process of switching can be time-consuming and cumbersome. Porting direct debits and recurring payments, redirecting incoming credits and closing legacy accounts are all common pain points. These frictions weaken demand elasticity, as consumers struggle to respond to better offers, thereby reducing the competitive pressure on incumbents. As a result, incumbents can maintain lower rates on legacy accounts while competing only at the margin for new customers. In practice, this dynamic leaves many depositors locked into lower rates, even when higher introductory or bonus offers are available. Thus, new entrants offering better rates to consumers than incumbents may struggle to secure a toehold in the market (ACCC, 2023^[40]).

27. For these reasons, policymakers and regulators have considered or pursued several strategies to address these barriers and increase contestability in deposit and lending markets (OECD, 2011^[2]).¹⁵ Moreover, the more products a consumer holds with one provider, the greater the customer inertia, reinforcing lock-in.¹⁶ For example, banks that offer a variety of retail products commonly link or bundle perks across products. Deposit accounts are often just one part of the bundle that consumers receive from banks. These accounts may be tied to preferential pricing on savings or loans. These bundles can deter single-product switching, may raise entry and expansion costs for challengers and limit the viability of single-product entrants (Anginer et al., 2019^[18]; BCA, 2023^[21]). The opacity of these arrangements further reduces mobility and blunts competitive pressure. Importantly, additional obstacles may also arise and further impede the switching process. For example, overdrafts on accounts can also lock consumers in, since outstanding unsecured debt or a lower credit score may complicate moving to an alternate provider (ComCom, 2024^[41]).

28. Switching costs and lock-in are also present for borrowers (Agarwal, Rosen and Yao, 2016^[44]). In many credit markets, oligopolistic structures and refinancing frictions, such as documentation burdens, collateral re-assessment or timing costs, dampen pricing pressure and slow competitive entry. Beyond transactional frictions, borrowers' lock-in is also heightened by the perceived value of longstanding ties, or relationship capital, with their bank (Vives, 2016^[4]). Asymmetric information about borrowers' creditworthiness may further entrench incumbents, where they hold proprietary data on projects and repayment capacity. This reduces screening costs and supports retention pricing, making it harder for challengers to compete.¹⁷

29. Further, because the provision of deposits and lending is often two-sided, with banks competing both to gather deposits and to extend credit, market dynamics on one side can entrench power on the other (OECD, 2025^[45]). Incumbents can fund loan growth at lower marginal cost through deposits, while challengers without deposit-taking authority must rely on costlier wholesale funding, securitisation, or bank partnerships. This can raise challengers' break-even rates and limit head-to-head rivalry in lending. Incumbents can also spread fixed and sunk costs across various areas, including technology, cybersecurity, data, reporting and marketing, to a wide customer base, thereby lowering their average cost relative to challengers. In turn, the fixed and sunk costs associated with entry and expansion, spanning compliance to marketing, may raise the minimum efficient scale required for challengers to compete.

30. As a result, to date, in many jurisdictions, the supply of deposits and credit is observed to be highly concentrated, with a small number of large incumbents serving most customers (Beyer, 2024^[46]). High concentration may be associated with weaker consumer outcomes, where there is limited choice and weak pricing pressure (Vives, 2016^[4]). Recent market studies confirm that concentrated retail banking markets, combined with switching frictions, slow and narrow the pass-through of savings and lending rates (ACCC, 2023^[40]; BCA, 2023^[21]; ComCom, 2024^[41]; FCA, 2023^[42]). This limits consumer benefits from competition and weakens the transmission of monetary policy, as rate changes are passed through more slowly and incompletely.

31. Greater competition enhances the responsiveness of the economy to interest rate changes, supporting macroeconomic management by central banks and improving the transmission of monetary policy (Lagarde, 2024^[47]). In competitive markets, firms react more swiftly to changes in financing costs, while higher concentration may blunt these effects, particularly for smaller firms (Ferrando et al., 2023^[48]). That is, one of the channels through which monetary policy can affect the real economy is the credit channel, with monetary easing affecting the cost of borrowing from banks (Byrne and Kelly, 2017^[49]).

32. A weakened or asymmetric pass-through can impact prudential objectives in several ways. When reductions in policy rates are not fully passed on to borrowers, lending rates remain high compared to funding costs, increasing repayment burdens and default risk, particularly for more leveraged households and SMEs. Over time, this can weaken banks' asset quality and amplify credit risk. More competitive lending markets, by facilitating faster and more complete pass-through to borrowers, may help contain such risks and improve loan performance (Byrne and Kelly, 2017^[49]; Van Leuvensteijn et al., 2008^[50]).

33. However, stronger competition may also compress bank margins and incentivise greater risk-taking, underscoring the need for appropriate prudential safeguards (Byrne and Kelly, 2017^[49]; Van Leuvensteijn et al., 2008^[50]). The effects of intensified competition on stability are complex and trade-offs may be present where banks cannot rely on "stable" deposits (Stenbacka and Takalo, 2019^[51]). For this reason, prudential regulations may emphasise liquidity or other prudential requirements for banks. As discussed in Section 3.2, competition, under appropriate prudential safeguards, can help alleviate weak pass-through and support overall financial stability.

34. In sum, in deposits and lending alike, these structural barriers to entry and expansion enable incumbents to sustain market power, raising rivals' costs and limiting entry and expansion. Lowering barriers in retail banking markets and enabling contestability can advance both prudential and competition

objectives in complementary ways, provided they are properly balanced and subject to prudential oversight, thereby enhancing diversification, efficiency and quality while promoting consumer welfare.

1.3.2. NBFi entry and opportunities for competition

35. Deposit and lending services help fuel the economy by channelling savings into productive investment through financial intermediation. However, across many jurisdictions, consolidation has been a persistent feature of these core banking services, coupled with limited new entry and the continued dominance of incumbent banks (Philippon, 2017^[52]). Traditionally, these core banking activities have been performed by licensed banks that collect deposits, extend loans and operate under the supervision of prudential authorities. In recent years, however, digitisation and technological innovation have begun to transform the competitive landscape. Digital challenger NBFIs, including neobanks, FinTechs and increasingly, BigTechs, have entered some of these core banking segments, reaching customers at scale through digital interfaces, often leveraging large user bases, data-driven credit scoring and embedded finance models (OECD, 2025^[45]).

36. It is worth noting that while NBFi entry can bring many benefits to competition, as addressed below, their growing role also introduces prudential and competition concerns. These concerns are often amplified by risks associated with digital ecosystem business models. From a competition perspective, these business models and data advantages may enable the leveraging of market power from adjacent digital markets into financial services (Ehrentraud et al., 2024^[53]; OECD, 2025^[45]).¹⁸ From a prudential perspective, while new competitors may improve efficiency in financial intermediation by offering greater product diversity and lower costs, they also pose systemic concerns, as their expansion may erode incumbents' profitability and increase risk-taking incentives (Carletti et al., 2020^[54]). Moreover, the growing reliance of banks and other financial providers on outsourced technology services from a handful of BigTechs raises operational third-party risks. BigTech ecosystems may warrant particular attention because a disruption in one part of the ecosystem can spill over into others, amplifying contagion across financial and non-financial services.¹⁹

37. Many new entrants initially avoid heavily regulated, capital-intensive activities such as deposit-taking. Instead, they focus on payment services first, which often fall outside the prudential perimeter, as they can carry lower risks and thus allow for rapid entry. This sequencing, beginning with payments, then expanding into credit, has become a common pathway to entry for FinTech and BigTech challengers. This new wave of entry has contributed to innovation and efficiency gains, lowered prices and expanded consumer choice, particularly in payments and lending, which can provide a pathway to expansion into broader retail banking markets (OECD, 2025^[45]). In this way, NBFi entry has enabled the progressive unbundling of core banking services, making at least some segments, such as lending, more efficient and innovative.

38. NBFi lending has the potential to circumvent some of the limitations of traditional credit markets, such as high intermediation costs. In this sense, NBFi lending may represent more than just a new delivery channel for credit: it has the potential to reconfigure the financial services value chain more broadly. By unbundling certain lending functions from traditional banks and enabling competition, NBFi lending can reshape market structure, foster dynamic entry and realign incentives toward consumer welfare. As discussed by Ehrentraud, Mure, Noble and Zamil (2024^[53]) the presence of these market participants can also enhance resilience by acting as a "spare tyre" for the financial system, mitigating variations in the supply of credit in times of banking sector distress.

39. The potential for NBFi expansion into deposit markets, or eventual full-fledged expansion across banking services, can similarly challenge traditional intermediation models and reshape market structure. Generally, by separating deposit-taking, payments and liquidity management from the balance sheets of incumbent banks, NBFIs can introduce new forms of competition into services historically characterised by concentration. Such entry and progressive unbundling can spur innovation in savings and credit

products, payment functionality, and user experience, thereby expanding consumer choice and potentially promoting more efficient allocation of liquidity within the system.

40. Yet, despite NBFi entry, many incumbent banks remain entrenched, with innovation often limited or channelled along their preferred paths, constraining the full benefits of competition and deterring the viability of NBFIs as a potential “spare tyre” to the financial system in times of stress (US Treasury, 2022^[55]; Bogaard et al., 2024^[56]; Ehrentraud, Garcia and Quevedo, 2020^[57]; OECD, 2025^[45]). Enduring challenges affecting competition in deposits and lending, which mute competitive pressure and enable incumbents to preserve their market power, include persistent structural and regulatory barriers to entry and expansion. Awareness of these persistent barriers may help inform policy design or enforcement responses, particularly as disproportionate or unnecessary prudential requirements may entrench incumbents, limiting or steering innovation that reduces the safeguards provided by the “spare tyre” role of independent NBFIs.

2 Competition challenges in prudential regulation

41. This Section discusses enduring challenges for competition in deposit and lending services stemming from prudential regulation. It examines aspects of prudential frameworks that may, in some cases, create unintended competition bottlenecks. In practice, any such bottlenecks may call for consideration, particularly in markets where competitive pressures are perceived to be weak. Approaches to balancing these considerations will necessarily vary across jurisdictions, reflecting differences in competitive landscapes, market structures, institutional settings and broader policy priorities. Therefore, the examples discussed illustrate tensions between prudential regulation and competition that policymakers may wish to consider in context. The potential opportunities for reconciling these objectives are addressed in Section 3. The Section also considers challenges arising from consolidation trends and concludes with a discussion of emerging issues in an increasingly digital and interconnected environment.

2.1. Regulatory barriers to entry and expansion

2.1.1. Retail deposits: competition considerations for prudential regulation

42. Retail deposits underpin both household and business wealth and serve as the foundation of the banking system's money-creation and credit functions. Disruptions to deposit-taking can have economy-wide effects. Managing liquidity risk is therefore central to prudential oversight, and deposit-taking is typically reserved for institutions that are licensed and supervised. Prudential safeguards are essential to maintaining trust and stability in banking. Without them, the system would be vulnerable to runs, contagion and excessive risk-taking (Vives, 2016^[4]). At the same time, licensing and related prudential requirements define the conditions of entry and, if not calibrated in a proportionate manner, may unintentionally limit contestability or slow expansion. Considering competition dynamics when designing or refining such frameworks can help ensure that prudential objectives are achieved effectively while avoiding unnecessary constraints on market entry, innovation, market dynamism, or consumer choice.

43. Licensing typically determines the associated prudential obligations attached to entry, such as (i) capital adequacy requirements, (ii) the scope of permissible activities and (iii) participation in deposit guarantee schemes, along with other associated governance and supervision standards. While this discussion focuses on these selected prudential obligations, it is not exhaustive. Other prudential requirements, such as liquidity ratios, can also influence entry and expansion, while the complexity of prudential frameworks may heighten compliance costs and affect contestability. At the same time, while this Section focuses on the substantive requirements linked to licensing, procedural aspects of the licensing process itself can also create bottlenecks to competition. This may occur where procedures are excessively lengthy, involve ad hoc or discretionary requirements, or lack legal certainty (OECD, 2023^[58]). The following examples illustrate potential competition bottlenecks arising from these selected substantive requirements in retail deposits, as well as areas where trade-offs between prudential regulation and competition may emerge, potentially requiring balancing where competition is assessed to be weak.

44. First, capital requirements are a key pillar of prudential frameworks that shape entry and contestability in deposit markets. They require banks or NBFIs to maintain a minimum level of capital to absorb losses and continue operating during periods of stress. By encouraging institutions to hold adequate buffers, capital requirements help maintain depositor confidence, reduce the likelihood of bank runs and ensure continuity in the provision of credit. They therefore play an important role in promoting financial stability.

45. At the same time, capital requirements set a critical threshold for market entry. That is, they represent a price tag to entry. If set too high or without regard to differences in risk profile or institutional size, initial requirements can represent disproportionate costs for smaller firms, tilting the playing field toward incumbents.²⁰ This can limit the number of firms that enter, insulating incumbents even when newcomers could offer more competitive rates or innovative products. Capital requirements can also advantage incumbents, where they represent unaffordable or disproportionate operational costs for new and smaller firms that cannot benefit from the same economies of scale (ACCC, 2023^[40]). Thus, when capital requirements are not proportionate, they may create undue bottlenecks to entry or expansion, warranting review, especially when competition is observed to be limited.

46. In most jurisdictions, capital requirements for deposit-taking institutions are based on the Basel Framework, developed by the Basel Committee on Banking Supervision (BCBS), which sets internationally agreed minimum capital standards for internationally active banks. Under this framework, total regulatory capital must equal at least 8% of risk-weighted assets (BCBS, 2025^[59]).²¹ The Basel standards provide a common benchmark for resilience and are a central reference point for prudential policy globally, helping to promote a level playing field in international banking. Jurisdictions, however, may differ in how they implement these standards for smaller or non-internationally active institutions that fall outside the Basel perimeter. Many jurisdictions apply proportionality principles to simplify requirements for such institutions while remaining consistent with Basel's overarching objectives.

47. For example, a mix of the following has been observed across jurisdictions: some apply the full Basel regime only to larger or systemically important banks, others exempt smaller institutions from selected provisions, while some adopt simplified or modified ratios across all providers. For example, full Basel standards are generally applied to mid-sized to large non-internationally active institutions with balance sheets of more than EUR 20-30 billion across many jurisdictions. Some countries apply larger thresholds, for example, the US and Brazil, where the full Basel regime is only applied to large or systemically important institutions (Hohl et al., 2018^[8]). In the European Union (EU), Switzerland and the US, smaller institutions are exempted from selected provisions and simplified or modified ratios are applied in India and Brazil (Castro Carvalho et al., 2017^[60]; BCBS, 2019^[61]; World Bank; BCBS, 2021^[62]).

48. These proportionality considerations can materially influence market structure and contestability (Hohl et al., 2018^[8]). Proportionate, risk-based capital frameworks, consistent with Basel standards, can help balance prudential and competition objectives. By tailoring requirements to institutional size, complexity and systemic relevance, authorities can reduce unnecessary entry barriers while preserving prudential safeguards. Section 3.1 discusses design options for calibrating capital requirements to promote contestability.

49. Second, in considering the scope of permissible deposit activities, it may be helpful to consider the associated risk profiles of differing products to assess whether prudential requirements may be calibrated to enable entry. Retail deposit products differ in maturity, liquidity and risk profiles from a prudential standpoint, which may justify differentiated licensing and supervisory requirements.²²

- Demand deposits, such as transaction or savings accounts, are payable on demand and can be withdrawn at any time, creating greater liquidity risk and exposure to runs.
- Term deposits, by contrast, are contractually locked in for a fixed period, providing a more stable funding base and thus reducing risks of mismatches.

- Interest rate structures associated with these different types of deposits also vary, reflecting their differences. Highly liquid accounts tend to offer negligible or variable returns, while term deposits pay higher fixed rates in exchange for reduced access to funds for a term.

50. Due to the distinct risk characteristics of deposit products, prudential frameworks may differentiate between types of deposits when considering permissible activities for NBFIs. Across most jurisdictions, monoline (single-activity) licenses are not available for demand deposits, with limited exceptions.²³ That is, accepting demand deposits is reserved for entities that hold a full banking license (authorising multiple activities, including deposit-holding and credit-extension). This reflects the heightened liquidity and co-ordination risks associated with demand deposits and their central role in the financial system.²⁴

51. However, some jurisdictions allow NBFIs to hold certain deposits, typically time deposits, which are perceived as less risky, subject to certain conditions within the prudential perimeter. For example, Germany's Banking Act allows NBFIs to accept term deposits.²⁵ In Colombia, NBFIs are allowed to issue certificates of deposit, a type of term deposit and in India, monoline licenses are available for term deposits, subject to certain conditions (Barakova, Ehrentraud and Leposke, 2024_[63]).²⁶ These regulatory approaches and how they enable competition are discussed further in Section 3.1.3. Table 1 summarises examples of jurisdictions with licensing regimes for NBI deposit-takers.

Table 1. Examples of jurisdictions with licensing regimes for NBI deposit-takers

Country	Name of license	Demand deposits	Term deposits	Risk-based capital requirements	Deposit guarantee scheme	Supervisory reporting
Argentina	Finance companies	Available	Available	Apply	Apply	Apply
Brazil	Finance companies		Available	Apply	Apply	Apply
Colombia	Financing companies		Available	Apply	Apply	Apply
Hong Kong (China)	Deposit-taking companies		Available	Apply		Apply
India	Non-bank financial companies		Available	Apply		Apply
Mexico	Popular financial Societies	Available	Available	Apply	Apply	Apply
New Zealand	Non-bank deposit takers		Available	Apply	Apply	Apply
Singapore	Finance companies		Available	Apply	Apply	Apply

Source: Adapted from Ehrentraud, J., Mure, S., Noble, E. and Zamil, R. (2024), Safeguarding the financial system's spare tyre: regulating non-bank retail lenders in the digital era, <https://www.bis.org/fsi/publ/insights56.pdf>; Mexico Financial License (2025), Mexico Licensing Guide 2025, <https://mexicofinanciallicense.com/wp-content/uploads/2025/08/Mexico-Licensing-Guide-2025.pdf>; New Zealand Financial Services Providers Register (2025), Applying to be a non-bank deposit taker (NBDT), <https://fsp-register.companiesoffice.govt.nz/help-centre/providing-licensed-or-certified-services/applying-to-be-a-non-bank-deposit-taker/>.

52. The rationale for expanding the scope of activities that NBFIs may undertake varies across these jurisdictions. It may reflect specific economic conditions, jurisdictional characteristics, or broader policy objectives, such as enhancing financial inclusion or diversifying market participation. Importantly, in these jurisdictions, where NBFIs are exceptionally authorised to take deposit-taking activities, they enter the prudential perimeter. This entails appropriate oversight and associated prudential obligations to preserve stability, including capital requirements, large exposure limits, creditworthiness assessments, fit-and-proper management assessments and supervisory reporting (Ehrentraud et al., 2024_[53]).

53. Where NBFIs are permitted to take certain types of deposits, jurisdictions may differ in approaches concerning the “in-or-out” choice on whether to extend deposit guarantee coverage, as well as how to set the appropriate levy amount.²⁷ These schemes ensure depositor funds up to a certain limit, protecting stability, confidence and mitigating run and contagion risks (EBA, 2024_[64]).²⁸ On the one hand, excluding deposit-taking NBFIs from these frameworks may pose prudential risk, with potential grave consequences for depositors. On the other hand, inclusion, depending on the type of institution, its risk profile, and the levy imposed, could be viewed as imposing an unnecessary, disproportionate, or overly costly entry barrier. Thus, this perimeter choice may benefit from balancing prudential and competition considerations. Section 3.1.1 discusses these trade-offs.

54. Third, additional requirements associated with licensing and authorisation may benefit from recalibration in light of digitisation and enabling cross-border competition. That is, requirements originally designed for traditional brick-and-mortar banks may not align with new or evolving business models. For example, local presence obligations, particularly those requiring a physical branch presence, may pose a barrier for digital-only or cross-border challengers. Thus, assessing alternative mechanisms, such as local incorporation, governance and operational oversight, may help achieve equivalent risk mitigation (Ehrentraud, Garcia and Quevedo, 2020_[57]). Section 3.1.3 discusses Hong Kong (China)’s adoption of digital-only bank licenses and the tailoring requirements in light of digitisation.

2.1.2. Retail lending: competition considerations for prudential regulation

55. Unlike deposits, lending is not unique to banks or even to financial institutions. In-kind loans occur whenever a consumer purchases a good or service without paying for it in full at the time of sale. Unlike deposit-taking, lending also does not necessarily entail the use of retail consumer funds. Many lenders finance their activities through equity, securitisation, or wholesale markets, rather than relying on retail deposits. As a result, the failure of a lender typically poses fewer direct risks to financial stability or depositor confidence. Nevertheless, prudential oversight of lenders can remain important where credit exposures are large, interconnected, or systemically significant. Accordingly, prudential frameworks for lenders differ across jurisdictions and across lending products.²⁹

56. Retail lending products can also be grouped into a few widely adopted categories that differ in risk profile, maturity, collateralisation and, consequently, in the prudential treatment they attract.³⁰ Broadly, loans may be secured, where collateral reduces credit risk but introduces valuation and maturity risks (e.g. mortgages), or unsecured, where credit and operational risks are higher but maturities are shorter and prudential requirements lighter.

57. The following discussion, while not exhaustive, highlights competition considerations in lending. First, in most jurisdictions, lending does not require deposit-taking capacity, so new entrants can often start as lenders only (Ehrentraud et al., 2024_[53]). That said, it may be informative to understand the potential challenges these new entrants may face due to their lack of deposit-taking capabilities. In some contexts, this analysis may inform whether specific types of lower-risk deposit products (e.g., time deposits) could be safely opened to support competition in markets where it is observed to be limited. This is discussed further in Section 3.1.3.

58. New entrants that offer lending services without a deposit-taking authority may face disadvantages in accessing capital. Such lenders typically rely on wholesale funding, securitisation, or partnerships with banks.³¹ Incumbent banks, by contrast, can use retail deposits to fund loan growth, often at a lower marginal cost. Consequently, challengers dependent on costlier funding sources may face higher break-even rates, constraining their ability to compete on loan pricing or offer longer-term credit.

59. Retail deposits provide multiple advantages compared to other funding sources. They are generally the most cost-effective form of funding and they strengthen customer relationships, including through cross-selling opportunities (ACCC, 2023_[40]). Loans funded by deposits may also entail lower

prudential risk, especially during periods of economic stress. This is because retail deposits are typically well diversified across many small account holders and are considered relatively stable in terms of liquidity.³² Prudential frameworks often reflect this by treating certain retail deposits as more stable in liquidity metrics (ACCC, 2023_[40]).³³ It is also worth noting that incumbent banks may benefit from advantages in accessing a wider range of funding sources beyond retail deposits.³⁴

60. Second, lending-only NBFIs in many jurisdictions are not subject to capital requirements unless designated as systemically important. This balanced approach can be beneficial to enable new entry and innovation.³⁵ Excessively broad capital requirements can create high barriers to entry for new or smaller lenders and, where applicable, limit the competitive pressure new entrants may exert on incumbents. Where prudential concerns are limited, because institutions do not take deposits and thus do not pose the same risks to financial stability, avoiding unnecessary entry costs through disproportionate capital requirements is thus appropriate.

61. Third, digitisation and NBFIs entry have expanded the range of unsecured credit products. NBFIs are a growing and important source of credit globally.³⁶ On the one hand, this may raise new considerations for risk management, as data increasingly substitutes for traditional collateral. On the other hand, research finds that using data to assess creditworthiness can reduce reliance on collateral values, potentially weakening the feedback loop through which swings in asset prices amplify credit booms and busts (Gambacorta et al., 2020_[65]). At the same time, reliance on data may introduce new sources of risk, including from data concentration, potentially reinforcing market power when access to large datasets becomes a key competitive advantage.

62. A prominent illustration of these dynamics is the rapid rise of buy-now, pay-later (BNPL) loans. BNPL offers an alternative to credit cards and bank loans, typically with shorter repayment terms and more flexible conditions.³⁷ BNPL providers challenge incumbents in retail credit, banks and card networks, by offering point-of-sale financing with lower or no interest, fewer fees and seamless digital experiences (OECD, 2025_[45]). They offer new ways to assess credit risk and creditworthiness, particularly for borrowers with limited traditional credit histories. This may broaden access and reduce risk, potentially improving stability (Tigges et al., 2024_[66]). Factors influencing competition between new entrants and incumbents include the level of bank concentration and the intensity of competition among new entrants (Vives, 2025_[67]). Generally, their presence can encourage traditional lenders to innovate, reduce fees, or enhance their digital offerings.

63. However, BNPL can raise prudential concerns, including those related to bank profitability, borrower overindebtedness, opaque risk transfer and limited credit loss provisioning. Bank profitability may decrease, particularly in markets where customers were underserved, prior to this new entry (Vives, 2025_[14]). Borrower overindebtedness may occur where consumers take on multiple BNPL obligations that are not reported to credit bureaus, obscuring aggregate household leverage and repayment capacity. Opaque risk transfer arises when BNPL providers sell or securitise receivables to third parties, potentially complicating oversight of the ultimate credit risk holders. Limited credit loss provisioning reflects the absence of prudential capital buffers or forward-looking requirements comparable to those applied to banks, which can leave BNPL firms vulnerable to losses during stress events (Amici, 2025_[68]; Morgan Stanley, 2025_[69]).³⁸

64. Rapid growth in the sector has further raised systemic concerns. As BNPL providers scale up and integrate with the broader financial system, including through partnerships with banks and reliance on securitisation, defaults could propagate through financial markets, heightening contagion risks. During economic downturns, the business model may prove particularly vulnerable to widespread defaults among consumers who have accumulated multiple BNPL obligations (Goulart, 2024_[70]). Until recently, BNPL largely remained outside most prudential perimeters, with many jurisdictions only recently extending oversight (Ehrentraud et al., 2024_[53]). Supervisory efforts increasingly aim to balance the benefits of innovation and financial inclusion with the need to monitor credit quality, leverage build-up and

interconnectedness with the regulated financial system. Box 3 discusses the evolution of the perimeter applicable to BNPL and how considering competition can help calibrate rules.

Box 3. Evolution of the prudential perimeter to BNPL credit and competition implications

The rapid expansion of buy now, pay later (BNPL) credit since 2019 has been driven by e-commerce growth and consumer demand for flexible, short-term financing. BNPL products, typically short-duration and interest-free, have often fallen outside the prudential perimeter. In many jurisdictions, this reflected product design that kept transactions below regulatory thresholds (e.g. loan size, duration, instalments). While this gap spurred entry, innovation and competitive pressure on traditional lenders, it also created prudential and consumer risks. As regulators expand the prudential perimeter to BNPL, balancing oversight with competition may be helpful, particularly through the use of competition impact assessments discussed in Section 3.

Australia

Reforms from 2023 brought BNPL under the Credit Act, requiring providers to obtain a licence and comply with responsible lending and disclosure rules. By introducing a new category of “low-cost credit contracts,” the framework aims to proportionally align obligations with BNPL risks while preserving entry and competition.

United Kingdom

HM Treasury’s final position and draft amendments to the Financial Services and Markets Act 2000 will subject BNPL to Financial Conduct Authority authorisation and reporting obligations, including data on credit quality, to enable effective supervision.

European Union

The amended Consumer Credit Directive (CCD2), applicable from 2026, removes exemptions for small loans, bringing BNPL within scope and enabling monitoring of BNPL portfolios and credit risk exposures. In its impact assessment, the European Commission (EC) noted that harmonisation would reduce market fragmentation, enhance cross-border competition and benefit smaller, concentrated national markets. The EC also recognised that increased compliance costs could raise barriers to entry for smaller providers or spur exit by currently unregulated providers.

Singapore

The 2022 BNPL Code of Conduct, developed by the Singapore FinTech Association under the Monetary Authority’s (MAS) guidance, sets standards to mitigate over-indebtedness. Though voluntary, an industry accreditation scheme encourages compliance. MAS continues to monitor developments and may consider a more prescriptive approach if market concentration or prudential risks increase.

From a prudential perspective, these reforms reflect a gradual extension of supervisory oversight, including licensing and reporting requirements in Australia, the EU and the United Kingdom, as well as a voluntary code in Singapore. All reforms aim to bring BNPL providers under frameworks that enable monitoring of credit risk, funding structures and the mitigation of over-indebtedness and systemic risk, while simultaneously ensuring consumers are adequately protected under consumer protection frameworks.

From a competition perspective, BNPL has arguably enhanced consumer choice, lowered credit costs, and increased pressure on incumbent banks and card issuers to innovate. However, as BNPL falls within the prudential perimeter, regulatory design may impact contestability, particularly where

incumbent institutions contribute to standard-setting or advocate specific rule designs. The policy challenge is to calibrate prudential rules to manage risks while not inadvertently deterring competition.

Source: Australian Government (2024), Buy Now Pay Later regulatory reforms, <https://treasury.gov.au/consultation/c2024-504798>; FCA (2025), Regulating Buy Now Pay Later (BNPL), <https://www.fca.org.uk/firms/regulating-buy-now-pay-later>; HM Treasury (2025), Regulation of Buy-Now, Pay-Later Government Response to Consultation, https://assets.publishing.service.gov.uk/media/6827536302662c6f8ec243c4/250516_-_BNPL_consultation_response_.pdf; European Commission, Commission staff working document impact assessment report accompanying the proposal for a Directive of the European Parliament and Council on consumer credits (2021), <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD%3A2021%3A170%3AFIN&locale=en>; European Commission (2023), Consumer Credit, https://commission.europa.eu/business-economy-euro/financial-services/retail-financial-services/consumer-credit_en; Consumer Financial Protection Bureau (2024), Truth in Lending (Regulation Z); Use of Digital User Accounts To Access Buy Now, Pay Later Loans, <https://www.federalregister.gov/documents/2024/05/31/2024-11800/truth-in-lending-regulation-z-use-of-digital-user-accounts-to-access-buy-now-pay-later-loans>; Federal Register, Interpretive Rules, Policy Statements and Advisory Opinions; Withdrawal, <https://www.federalregister.gov/documents/2025/05/12/2025-08286/interpretive-rules-policy-statements-and-advisory-opinions-withdrawal>; Monetary Authority of Singapore (2025), Written reply to Parliamentary Question on reports of non-compliance with Buy Now Pay Later (BNPL) Code of Conduct and data on BNPL customers, <https://www.mas.gov.sg/news/parliamentary-replies/2025/written-reply-to-parliamentary-question-on-reports-of-non-compliance-with-bnpl-code-of-conduct>; Monetary Authority of Singapore (2022), Reply to Parliamentary Question on "Buy Now Pay Later" Schemes, <https://www.mas.gov.sg/news/parliamentary-replies/2022/reply-to-parliamentary-question-on-buy-now-pay-later>; Ehrentraud, J; Mure, S; Noble, E; Zamil, R (2024), Safeguarding the financial system's spare tyre: regulating non-bank retail lenders in the digital era, <https://www.bis.org/fsi/publ/insights56.pdf>; Cornelli, G; Gambacorta, L; Pancotto, L (2023), Buy now, pay later: a cross-country analysis, https://www.bis.org/publ/qrpdf/r_qt2312e.htm; Xavier Vives (2025), FinTech Competition in Lending <https://wifpr.wharton.upenn.edu/wp-content/uploads/2025/10/WIFPR-FinTech-Competition-in-Lending-Vives.pdf>.

2.2. Trends toward consolidation and entrenchment

65. There is a delicate balancing act between safeguarding stability and preserving competitive market structures. As discussed in Section 1.2, tensions and trade-offs arise between prudential and competition authorities, particularly when reviewing mergers (which across many jurisdictions is within the purview of both authorities) or in the context of state support, intervention, or state aid (which may fall within the purview of competition authorities in certain jurisdictions). Mergers, while sometimes justified on efficiency or resilience grounds, can contribute to longer-term trends toward consolidation and entrenchment, substantially lessening competition, if not carefully assessed. State support may likewise entrench incumbent advantages by unlevelling the playing field, lowering funding costs in favour of incumbents and discouraging new entry or expansion. Importantly, while tensions are present, both mergers and state support can lead to TBTF institutions and risk financial stability, thereby raising competition and prudential risks, underscoring the need for balancing and co-operation.

66. The tensions and trade-offs between prudential and competition objectives may be particularly pronounced during periods of financial stress, when prudential authorities may support mergers or other measures to maintain stability short term, even where such interventions risk reducing competition in the short and long term (OECD, 2011^[26]; 2021^[31]). For example, in the past, competition concerns regarding mergers have been sidelined during crises. Where crisis-driven mergers have occurred, their anticompetitive effects often far outlast the crisis. Box 4 discusses a previous case in which competition concerns were set aside in a merger during a crisis.

Box 4. The merger of Lloyds and HBOS in the United Kingdom

The global financial crisis brought financial stability and competition principles into direct conflict in the proposed Lloyds Banking Group (Lloyds or LBG) acquisition of Halifax Bank of Scotland (HBOS). In late 2008, in response to great market stress, Lloyds agreed to acquire HBOS. The merger was approved in 2009, despite the Office of Fair Trading's (OFT) opinion that competition problems would flow from the merger.

The OFT advised the Secretary of State to refer the deal for a full competition investigation, citing substantial concerns regarding retail demand deposits, with the merged firm expected to reach around a 30% market share and the loss of a key challenger in Scottish SME banking. In parallel, the Bank of England, the Financial Services Authority (FSA) and HM Treasury urged approval on grounds of financial stability. The Government responded by adding “the stability of the United Kingdom (UK) financial system” to the statutory public-interest grounds to be considered under the Enterprise Act 2002, applicable to merger control. The Secretary of State thus overrode the OFT's recommendation and cleared the merger on that basis. Shortly afterwards, alongside broader crisis measures, the state injected capital, taking an equity stake in Lloyds.

As a result of the merger, HBOS, the main challenger to the four large established banks in Scotland, was eliminated. As later confirmed by the Competition and Markets Authority's (CMA) 2016 retail banking market investigation, the combined market share of the largest four banking groups increased as a result of Lloyds TSB's acquisition of HBOS. Even earlier, in 2010, Sir John Vickers underscored that “the takeover did pose clear risks to competition.” He added that alternative solutions would have been more pro-competitive and that it “would appear to have been a mistake to waive normal merger law . . . Relaxation of competition law was not a good way to help financial stability in this case and as the subsequent problems of LBG have shown, it may have worsened it.” He concluded that, “there is good reason to believe that there needs to be more competition in banking, not less, especially in view of the competitively impaired post-crisis structure.”

Source: Vives, X. (2016), *Competition and Stability in Banking: The role of regulation and competition policy*, Princeton University Press; CMA (2016), Retail banking market investigation, <https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf>; The Enterprise Act 2002 (2008), Specification of Additional Section 58 Consideration Order, <https://www.legislation.gov.uk/ukSI/2008/2645/article/2/made>; Department for Business, Enterprise & Regulatory Reform (2008), Decision by Lord Mandelson, the Secretary of State for Business, not to refer to the Competition Commission, the merger between Lloyds TSB Group plc and HBOS plc under Section 45 of the Enterprise Act 2002, <https://data.parliament.uk/DepositedPapers/Files/DEP2008-2685/DEP2008-2685.pdf>; House of Commons (2008), The Lloyds-TSB and HBOS Merger: Competition Issues, <https://researchbriefings.files.parliament.uk/documents/SN04907/SN04907.pdf>; Vickers, J (2010), Central Banks and Competition Authorities: Institutional comparisons and new concerns, <https://www.bis.org/events/conf100624/vickerspaper.pdf>.

67. Historically, prudential considerations limited the application of competition law to the banking sector. In several jurisdictions, banks were shielded from general merger control on the grounds of systemic stability or sectoral supervision. In France, for instance, bank mergers have been subject to ordinary merger control only since 2003 (Cœuré, 2025^[15]). Today, across many jurisdictions, merger control by competition authorities and prudential regulators applies to bank mergers, with close cooperation between the two. Box 5 provides an example of how this co-ordination works in practice in the US.

Box 5. Review of banking mergers in the United States

The Antitrust Division of the Department of Justice independently assesses the competitive effects of proposed bank mergers under the antitrust laws while co-ordinating closely with the federal banking agencies. The Antitrust Division's review focuses exclusively on competitive factors and does not address the other statutory considerations applied by banking agencies (though competition issues may influence those broader assessments). Importantly, as discussed below, the Antitrust Division may consider the failing-firm defence in its review. Once the Antitrust Division concludes its review, it provides a competitive factors report to the relevant banking agency, which may take those findings into account in its prudential decision-making. If the banking agency grants approval, the Antitrust Division may, at its discretion, challenge the legality of a merger following such approval. A legal challenge by the Antitrust Division suspends the effectiveness of that approval pending federal court review.

Source: US Department of Justice (2024), 2024 Banking Addendum to 2023 Merger Guidelines, <https://www.justice.gov/atr/media/1368576/dl>; US Department of Justice (2023), 2023 Merger Guidelines, <https://www.justice.gov/atr/merger-guidelines/rebuttal-evidence>.

68. However, certain jurisdictions retain provisions implemented after the global financial crisis that allow for the possibility of not submitting mergers to competition authority review. Box 6 discusses a recent such case in Switzerland.

Box 6. The merger of UBS and Credit Suisse in Switzerland

In March 2023, Swiss authorities announced that UBS Group AG would acquire Credit Suisse Group AG in an emergency transaction aimed at restoring confidence in the financial system. The Swiss Financial Market Supervisory Authority (FINMA) approved the deal, noting that it would “secure financial stability and protect the Swiss economy.” To facilitate the takeover, the Swiss National Bank (SNB) provided up to CHF 100 billion in liquidity assistance and the Swiss Confederation offered an additional CHF 100 billion guarantee against potential losses.

The transaction was exempted from the ordinary merger-control process under Article 10(3) of the Swiss Cartel Act (CartA). Introduced after the 2008 crisis, this provision allows the government to bypass full Competition Commission (COMCO) review when a bank merger is “required in the interest of the creditors.” In such cases, COMCO may issue only non-binding advice and FINMA's approval suffices for completion. The exemption was invoked in this case to expedite the rescue.

In its subsequent public comments, COMCO acknowledged potential competition concerns, particularly in wealth management, corporate banking and investment banking, but confirmed that it had been limited to an advisory role under the emergency procedure. In June 2024, FINMA formally concluded its ex-post review, finding that the merger “does not eliminate effective competition in any market segment” and therefore closed the case without conditions.

Commentators have since observed that the merger created a state-induced institution with significant market power, underscoring that the exclusion of merger control has non-negligible consequences for competition. Time will tell how the merger will affect stability and competition in the long term. However, as underscored by the Financial Stability Board in its Peer Review of Switzerland and discussed further in Section 3, enhancing resolution frameworks can provide an alternative to crisis mergers and address material impediments to resolvability. Importantly, recent analysis further warns that resolution practices

relying on large incumbents as “white knights” can stabilise markets in the short term but risk reinforcing concentration and reducing contestability, underscoring the importance of ensuring that resolution frameworks themselves do not perpetuate market power.

Taken together, the case illustrates the tension between stability and competition objectives in emergency interventions. While the exemption under Article 10(3) CartA enabled swift action to avert a systemic crisis, the resulting consolidation and potential entrenchment of market power highlight the importance of considering alternative measures or ensuring that exceptional measures remain proportionate, time-bound and subject to transparent ex post assessment.

Source: FINMA (2024), Merger of UBS and CS: FINMA concludes control procedure, <https://www.finma.ch/en/news/2024/06/20240619-mm-zusammenschluss-ubs-cs/>; Heynen, P; Haekens, J (2023), The Crédit Suisse-UBS Merger: Ceci N'est Pas Competition Law, <https://legalblogs.wolterskluwer.com/competition-blog/the-credit-suisse-ubs-merger-cest-nest-pas-competition-law/>; Hirt, O (2023), Swiss regulator rules out UBS antitrust action over Credit Suisse deal, <https://www.reuters.com/markets/deals/swiss-financial-regulator-closes-ubs-antitrust-probe-after-credit-suisse-merger-2024-06-19/>; FINMA (2023), FINMA approves merger of UBS and Credit Suisse, https://www.finma.ch/en/-/media/finma/dokumente/dokumentencenter/8news/medienmitteilungen/2023/03/20230319-mm-cs-ubs.pdf?hash=47C921C769CE0100247843DD1E86D106&sc_lang=en; Baumann, C (2024), Comco Demands Deeper Investigation Into UBS Market Power, <https://www.finews.com/news/english-news/61615-comco-finma-ubs-market-power-dominance-obligations>; Financial Stability Board (2024), Peer Review of Switzerland, <https://www.fsb.org/2024/02/peer-review-of-switzerland/>; Coeuré, B, H Huizinga, E König, J Krahen and J Schlegel (2024), Policy Insight 134: Winners and losers in bank resolution: Recent examples and a modest reform proposal, CEPR Policy Insight No 134, CEPR Press, Paris & London. <https://cepr.org/publications/policy-insight-134-winners-and-losers-bank-resolution-recent-examples-and-modest>.

69. As discussed in Section 1.3, concentration, coupled with limited entry and entrenchment of incumbent banks, has been a persistent feature across jurisdictions (Philippon, 2017^[52]). Successive merger waves have increased concentration across jurisdictions.³⁹ Evidence from past decades shows that while mergers may sometimes deliver benefits, efficiency gains have been modest, while market power motives are often the dominant rationale for mergers (Federal Reserve, 1999^[71]). DeYoung and Whalen (1999^[72]) underscore that consolidation may often have been driven by the pursuit of TBTF status and that it can harm borrowers, depositors and other stakeholders. Philippon (2017^[52]) argues that this has contributed to poor overall efficiency and excessive rents.

70. More recently, concerns have emerged that consolidation trends extend beyond traditional banking, where incumbents acquire FinTechs and other innovators rather than developing competing technologies internally (Marty and Warin, 2020^[73]; AdC, 2021^[74]). Such acquisitions, sometimes described as “killer acquisitions” or “reverse killer acquisitions,” may allow incumbents to absorb potential rivals and slow or steer disruptive innovation, entrenching market power across adjacent markets (Crawford, Valletti and Caffarra, 2020^[75]; Cunningham et al., 2021^[76]; OECD, 2020^[77]). While some transactions have promoted diversification or resolved failing institutions, efficiency gains have not always been passed through to consumers. In sum, consolidation reshapes market structures but has not consistently improved performance (DeYoung and Whalen, 1999^[72]). Box 7 discusses evidence from Japan.

Box 7. Evidence of bank mergers from Japan

In the late 1990s, Japan experienced the failures of large banks. As financial conditions deteriorated, several of the remaining institutions chose to merge, seeking to strengthen efficiency and resilience in order to avert further failures. At the time, with capital positions weakened by non-performing loans and declining asset values, consolidation was viewed as a means to stabilise balance sheets through economies of scale.

However, ex post evidence underscores that these mergers generated few measurable efficiency gains and did not materially improve the financial soundness of the institutions involved. Empirical analyses of the period reveal two key findings:

- Financial soundness was largely inherited from pre-merger institutions. That is, sound banks merged into sound entities, while weaker banks remained fragile post-merger, suggesting that consolidation itself added little intrinsic value.
- Some merged banks experienced a decline in distance-to-default immediately after consolidation, implying that the mergers may have weakened rather than strengthened solvency in the short term.

These findings are consistent with the view that many of the mergers were motivated less by efficiency gains than by a desire to benefit from an implicit too-big-to-fail policy. Alternatively, they may reflect an implementation gap: where mergers pursued for efficiency failed to achieve genuine operational improvements. Overall, Japan's experience illustrates the limitations of consolidation as a prudential policy response during systemic stress.

Source: Harada, K. and Ito, T. (2008), Did Mergers Help Japanese Mega-Banks Avoid Failure? Analysis of the Distance to Default of Banks, <https://www.nber.org/papers/w14518>.

71. That said, at times, emergency combinations can be the least-bad option to preserve stability in the short term. This is why competition-based merger control can consider the risk of an institution's failure under the failing-firm defence. In other words, competition law recognises, through the failing-firm defence, that a merger may be the "lesser of two evils" (SCOTUS, 1974^[78]).

72. The failing-firm defence, as adopted by many jurisdictions, generally requires three cumulative conditions: (i) exit is imminent absent the merger; (ii) no less anti-competitive alternative exists; and (iii) the assets would otherwise leave the market (OECD, 2010^[79]). In practice, this means that a merger that would otherwise substantially lessen competition may proceed if these strict conditions are all met. However, because mergers can significantly shape competition in the long term, the bar for invoking this defence should remain high and carefully scrutinised. Lowering the standard to, for example, weaker claims based on "flailing firm" or "weakened competitor" arguments risks normalising consolidation and embedding market power. This underscores the need for close co-operation between prudential and competition authorities to avoid zero-sum trade-offs, as discussed in Section 3.

73. While consolidation is relevant to competition and prudential objectives more broadly, consolidation and the potential for entrenchment also give rise to potential TBTF institutions. As aforementioned, studies have found that consolidation may often have been driven by the pursuit of TBTF status (DeYoung and Whalen, 1999^[72]; Harada, 2008^[80]). TBTF policies constitute a form of state aid because there is an implicit guarantee of help. TBTF institutions are of concern to both prudential regulators and competition authorities because they distort stability and competition. Prudentially, the distress of a very large or highly interconnected firm endangers the continuity of critical functions, magnifies contagion and complicates resolution. From a competition perspective, expectations of public support can operate like an implicit subsidy, unlevelling the playing field by reducing funding costs for incumbents and weakening pressure from smaller rivals (Vives, 2016^[4]).

74. In other words, when state support disproportionately benefits incumbents, it can unlevel the playing field by conferring selective advantages, such as lower funding costs or explicit guarantees, that are not equally available to challengers. Such interventions can undermine the principle of competitive neutrality, which seeks to ensure that public measures do not distort market competition or favour specific firms (OECD, 2024^[81]). Rather than picking winners and losers in the market, which can misallocate resources and undermine stability and contestability, competitive neutrality ensures competition is not distorted.

75. This distortion can be amplified when past or prospective state aid generates moral hazard. By contrast, competitive markets, supported by rigorous merger control, limits on state aid and credible exit paths, can reduce the market power of any single firm and compress the rents that may make TBTF status attractive. That is, competition policy can be part of the solution to the TBTF problem by avoiding the

consolidation of an anticompetitive market structure that leads to a TBTF entity, or by assessing state aid to mitigate distortions to competition. Box 8 discusses the EU's use of the latter. Accordingly, prudential and competition authorities share a common objective: to prevent the rise of TBTF institutions, preserve a level playing field and ensure that failures are manageable without distorting market outcomes.

Box 8. The European Union's approach to state aid control

Under Articles 107–109 of the Treaty on the Functioning of the European Union (TFEU), public support granted by a Member State or through state resources must not distort competition or trade within the EU single market by favouring certain undertakings or the production of particular goods. “State aid” encompasses any selective advantage provided by public authorities, such as grants, state-guarantees or interest-free loans, tax relief, or access to goods and services on preferential terms.

The EC is responsible for assessing whether such measures are compatible with the internal market. Aid may be authorised where it serves an objective of common interest, such as preserving financial stability, provided the measure is necessary and proportionate and is accompanied by safeguards to limit distortions of competition.

During and after the global financial crisis, the EC applied these principles through a series of crisis communications, including the 2013 Banking Communication. This aimed to ensure that support for financial institutions was strictly limited to what was needed to maintain stability and often combined restructuring and behavioural commitments to mitigate competitive distortions and moral hazard. By controlling and monitoring State aid, the EC aims to help maintain a level playing field in the EU internal market, ensuring that firms compete on their merits rather than on preferential public support.

Since then, these principles have been reinforced through the Bank Recovery and Resolution Directive (BRRD), which hardwires resolution rules into EU law to reduce reliance on taxpayer-funded rescues. However, the BRRD's implementation has at times been uneven, with several bank resolutions handled under national insolvency regimes rather than EU procedures. This has raised concerns about consistency and competitive neutrality.

Source: Official Journal of the European Union (2013), Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis (‘Banking Communication’), [https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013XC0730\(01\)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013XC0730(01)); European Commission (2025), State Aid, https://commission.europa.eu/topics/competition/state-aid_en; Humblet, M; Dutilleul, W (2025), State Aid in Financial Services: An Overview of EU Policy, <https://www.concurrences.com/en/bulletin/special-issues/state-aid-financial-services/state-aid-in-financial-services-an-overview-of-eu-policy>; Vives, X. (2016), Competition and Stability in Banking: The role of regulation and competition policy, Princeton University Press; Official Journal of the European Union (2014), Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms, <https://eur-lex.europa.eu/eli/dir/2014/59/oj/eng>; Famfollet, J; Sankotová, E (2020), Italian bank crisis: Flexible application of BRRD rules, or a bailout in disguise?, <https://doi.org/10.2478/revecp-2020-000>; Asimakopoulos, I and Howarth, D (2022), Stillborn Banking Union: Explaining Ineffective European Union Bank Resolution Rules; <https://onlinelibrary.wiley.com/doi/pdf/10.1111/jcms.13212>.

2.3. NBF entry through bank-partnerships

76. Partnerships between NBFIs and banks, including white-labelling arrangements with BigTechs and FinTechs, where a licensed bank provides the regulated balance-sheet and infrastructure while the NBF partner controls the customer interface under its own brand, have become increasingly common (OECD, 2025^[45]). A potential consideration arising from the widespread adoption of partnerships is whether prudential requirements may be unnecessarily channelling new entrants into partnerships, by limiting the possibility of independent entry and expansion, thereby creating both competition and prudential concerns.

77. Table 2 illustrates BigTech and large FinTech service offerings, mapping their licensing and partnership models across jurisdictions. Importantly, partnerships between smaller FinTechs and banks are even more frequent, particularly in the provision of deposit services (Barakova, Ehrentraud and Leposke, 2024^[63]). For example, in the US, a 2022 study found that almost two-thirds of banks had established at least one partnership with a FinTech firm over the preceding three years, a share that is expected to continue rising (US Treasury, 2022^[55]; Synctera, 2022^[82]).

Table 2. BigTech and large FinTech licenses and pathways to entry across jurisdictions

Tech firms	Bank partnership: Deposits	Bank partnership: Lending	Independent entry: Deposits	Independent entry: Lending	Banking license
Apple	US			UK, US	
Amazon		EU, India, US		UK, US	
Ant Group		People's Republic of China (China)		China, UK	China, Hong Kong (China), Singapore
Google		India			
Paypal	US	India, US			EU
Mercado Libre			Mexico*	Argentina, Brazil, Colombia, Mexico	
Meta		India			
Nubank			Mexico**	Brazil, Mexico**	Mexico
Tencent		China			China, Hong Kong (China)

Note: (*) In payments, where funds are not swept automatically to a user's linked deposit account (i.e., pass-through mobile payment services), providers may earn money when users store funds on their platforms by holding and investing funds (i.e., staged mobile payment services). In this way, staged payment services can be perceived as a form of deposit. Use of staged mobile wallets as deposit-like products is prevalent in jurisdictions like Mexico. Thus, based on prudential policy objectives, staged mobile payments may be subject to more oversight and insurance requirements than pass-through mobile payments. (**) In 2025, Nubank received a full banking license to operate in Mexico; prior to that, it held a deposit-taking license.

Source: Adapted from Barakova, I., J. Ehrentraud and L. Leposke (2024), A two-sided affair: banks and tech firms in banking, <https://www.bis.org/fsi/publ/insights60.htm>; Nubank (2025), Nu Mexico receives banking license approval, paving the way for product portfolio expansion and increased financial inclusion, <https://international.nubank.com.br/company/nu-mexico-receives-banking-license-approval-paving-the-way-for-product-portfolio-expansion-and-increased-financial-inclusion/>; OECD (2025), "Competition in mobile payment services", *OECD Roundtables on Competition Policy Papers*, No. 324, OECD Publishing, Paris, <https://doi.org/10.1787/0ce6b5d3-en>.

78. While partnerships between banks and NBFIs can accelerate innovation and broaden consumer choice, they may also raise both competition and prudential concerns. From a competition perspective, they may reinforce incumbents' advantages, as challengers depend on the very institutions they aim to disrupt. This dependency can reduce competitive intensity, enable collusion and may facilitate anticompetitive practices such as tying, bundling, leveraging or foreclosure (OECD, 2025^[45]). Competitive intensity is particularly diminished because challengers often compete at the margins rather than directly with incumbents. Thus, partnerships mitigate the competitive benefits of new entry by shifting the focus from rivalry to co-operation. This can also lead to innovation being limited or steered toward incumbent-defined paths, thereby reinforcing entrenched market power.

79. Partnerships also raise prudential concerns. Partnerships blur the boundary between regulated and unregulated activity, creating interdependencies and shifting risks across the regulatory perimeter. They also complicate prudential supervision by reducing transparency about where risks ultimately reside (BCBS, 2025^[83]). In practice, prudential blind spots and weakened competition can reinforce one another: opacity obscures risk allocation, while dependency entrenches incumbents, including by potentially giving them leverage over market access under the guise of stability.⁴⁰

80. Banks benefit from deep expertise in prudential regulation and compliance that new entrants can struggle to replicate. Regulatory familiarity enables incumbents to absorb compliance costs and maintain their central role in credit and deposit markets. As a result, many new entrants in deposits and lending increasingly avoid being subject to prudential regulation by relying on partnerships with banks for access to regulated financial activities. In this sense, prudential regulations perceived as burdensome, restrictive, or too capital-intensive may channel new entry into partnerships. That is, partnerships can be a direct consequence of the comparative advantages that incumbents retain in regulatory compliance (Feyen et al., 2021^[84]). Thus, considering simplification, proportionate and predictable requirements can help preserve space for independent, well-supervised entry. Box 9 discusses the UK’s “Strong and Simple” prudential framework.

Box 9. The United Kingdom’s “Strong and Simple” prudential framework

Between 2023 and 2025, the Bank of England and Prudential Regulation Authority (PRA) set out and progressed the “Strong and Simple” prudential framework through final rules and consultation. The package of measures is aimed at maintaining financial sector stability while offering new opportunities for competition and growth. The Prudential Regulation Authority (PRA) proposed these measures to mitigate the ‘complexity problem’ that may arise when the same prudential requirements are applied to all firms of different sizes and business models by simplifying the prudential framework. As acknowledged by the PRA in its review of its prudential frameworks, complex rules may deter smaller firms from growing in size or breadth of activities, potentially reducing competition. The updated regime aims to advance the PRA’s safety and soundness and secondary competition objectives.

According to the PRA, the Strong and Simple framework forms part of a phased approach to delivering a more proportionate prudential regime for smaller firms, while maintaining alignment with international standards such as Basel, where appropriate. The framework aims to simplify compliance and reduce unnecessary regulatory burden without compromising the resilience of individual institutions or the wider financial system

Source: Bank of England (2024), Strong and Simple – completing the picture - speech by David Bailey, <https://www.bankofengland.co.uk/speech/2024/september/david-bailey-speech-at-building-societies-association>; Bank of England (2023), Operating the Small Domestic Deposit Taker (SDDT) regime, <https://www.bankofengland.co.uk/prudential-regulation/publication/2023/december/small-domestic-deposit-taker-regime>; Bank of England (2024), The Strong and Simple Framework: The simplified capital regime for Small Domestic Deposit Takers (SDDTs), <https://www.bankofengland.co.uk/prudential-regulation/publication/2024/september/strong-and-simple-framework-the-simplified-capital-regime-for-sddts-cp>; Bank of England (2023), The Strong and Simple Framework: Scope Criteria, Liquidity and Disclosure Requirements, <https://www.bankofengland.co.uk/prudential-regulation/publication/2023/december/strong-and-simple-framework-policy-statement>.

3 Opportunities to enhance balance and complementarities

81. This Section first discusses considerations potentially relevant to balancing prudential and competition objectives, including the in-or-out trade-off, exit frameworks and competition considerations for licensing, including capital adequacy requirements, the scope of permissible activities and participation in deposit guarantee schemes. It then discusses concrete examples of how competition policy and enforcement may support prudential objectives. The Section concludes by highlighting potential approaches to strengthen co-operation between prudential regulators and competition authorities.

3.1. Considerations for balancing prudential regulation and competition

3.1.1. Addressing the “in or out trade-off”

82. A key challenge in aligning prudential design with competition is the “in-or-out” trade-off: whether new entrants fall within or outside the supervisory perimeter. If the perimeter is too narrow, large or rapidly growing new players may remain outside prudential oversight, creating blind spots and potential systemic vulnerabilities. Conversely, if the perimeter is too broad, all entrants may face disproportionate obligations, regardless of their size, business model, or risk profile, which could discourage entry and entrench incumbents. The effectiveness of this balance may benefit from approaches that move beyond binary choices and that are regularly reassessed. Box 10 discusses activity-based vs. entity-based regulations.

Box 10. Activity-based vs. Entity-based regulation

Policymakers are increasingly debating the merits of activity-based versus entity-based regulation. Activity-based regulation applies the same requirements to a service, regardless of who performs it. Such frameworks are often viewed as promoting consistency across entities and limiting opportunities for regulatory arbitrage between banks and non-banks. Yet, without sufficient proportionality, activity-based regimes may also place greater compliance demands on smaller or less complex providers, potentially affecting market entry. Entity-based regulation, by contrast, imposes requirements on specific firms or types of institutions, reflecting their scale, complexity and systemic interconnectedness. This model can capture risks arising from the combination of multiple activities within large groups and can extend oversight to significant new entrants without necessarily subjecting all participants to the same prudential obligations.

Each approach has distinct strengths and limitations. Activity-based regulation tends to enhance consistency across providers of similar services but may not fully capture intra-group linkages that can amplify shocks across business lines. It may also affect market dynamics if rules are calibrated primarily with larger incumbents in mind. Entity-based regulation can address some of these risks but may lead to differences in treatment across providers, particularly if only certain firms (such as BigTechs) are

designated for entity-level oversight while others offering similar services remain under activity-based rules. That said, in some circumstances, differentiation in regulatory treatment between larger and smaller entities has been considered necessary to safeguard contestability, though this requires careful calibration and periodic review. By imposing obligations on specific firms (usually those with significant market power), such frameworks can influence competitive dynamics by shaping conditions for market access and entry.

In practice, many prudential regimes combine elements of both approaches, and the relative emphasis placed on each can affect the balance between competition, innovation and prudential outcomes. A combination of the two is often implemented through proportionate thresholds and adaptive frameworks. In some jurisdictions, activity-based requirements provide a common baseline for entities performing similar functions, while entity-based measures are applied to firms that meet defined criteria related to scale, interconnectedness, or systemic relevance. In this way, smaller participants operate under proportionate expectations, while larger entities (whose distress could have broader systemic effects) are subject to more intensive oversight. Regular review of such frameworks helps ensure that the regulatory perimeter remains appropriate in light of market developments and emerging risks.

Source: Borio, C; Claessens, S; Tarashev, N (2022), Entity-based vs activity-based regulation: a framework and applications to traditional financial firms and big techs, <https://www.bis.org/fsi/fsipapers19.pdf>; OECD (2024), Competitive Neutrality Toolkit: Promoting a Level Playing Field, OECD Publishing, Paris, <https://doi.org/10.1787/3247ba44-en>.

83. Static rules risk creating new loopholes or unnecessarily discouraging market entry or expansion. In turn, dynamic approaches, such as licensing that scales requirements as firms grow, or periodic reviews of systemic designations, may better align prudential objectives with competition. For example, certain jurisdictions apply scale-based or proportional prudential regimes for NBFIs. Box 11 discusses the approaches of India and Brazil.

Box 11. Scale-based prudential regimes

India

The Reserve Bank of India (RBI) introduced a scale-based regulatory (SBR) framework for NBFIs in 2021, which came into effect in 2022 and was updated in 2023. The SBR framework organises NBFIs into four layers, depending on their activity, asset size and perceived riskiness.

- Base layer: Smaller non-deposit-taking NBFIs fall into the base layer and face simpler requirements, such as a leverage ratio and basic disclosure rules.
- Middle layer: All deposit-taking NBFIs, as well as larger non-deposit-taking NBFIs above INR 1,000 crore in assets and activity-based lenders such as housing finance and microfinance companies, are placed in the middle layer, subject to capital, liquidity, provisioning and governance standards.
- Upper layer: This layer captures systemically significant NBFIs, including the ten largest by assets, which are required to meet bank-like prudential requirements with adjustments, including an equity ratio of at least 9%, internal capital adequacy assessment processes and large exposure limits.
- Top layer: This layer is expected to remain empty but can be activated at the RBI's discretion if particular NBFIs are seen as generating excessive systemic risks, triggering higher capital requirements and enhanced supervisory engagement.

By tailoring obligations to the scale and activity of NBFIs, the SBR framework allows smaller entities to operate under proportionate requirements while ensuring that systemically important firms are subject to more robust safeguards.

Brazil

Brazil applies a system-wide proportionality framework to all credit institutions, including NBFIs retail lenders. Under the Central Bank of Brazil's segmentation approach, institutions are classified into five segments (S1-S5), based on their systemic importance and international activity. Prudential requirements, including capital, liquidity, governance, risk management and large exposures, apply to all, but with increasing stringency by segment. The largest, most systemically important institutions (S1 and S2) face Basel-aligned requirements, while smaller non-banks with simple risk profiles (S5, less than 0.1% of GDP) face simplified obligations. Macroprudential measures, such as the countercyclical capital buffer, apply to NBFIs in S1–S4, where relevant, ensuring that larger NBFIs are incorporated into the macroprudential perimeter. In addition, recent reforms, with phased implementation from 2023 to 2025, have expanded group-wide prudential regulation to include new financial conglomerates, including those involving payment institutions. This proportional segmentation aims to avoid a “one-size-fits-all” approach while ensuring that systemic entities are subject to prudential oversight.

These approaches provide illustrative examples of flexible pathways for embedding proportionality into NBFIs prudential regulation and enabling competition. India's SBR is tailored specifically for NBFIs, with the flexibility to escalate requirements if systemic risks arise. Brazil's segmentation applies a single, proportional prudential framework across all institutions, including banks and NBFIs. Both regimes aim to safeguard financial stability and mitigate the risks of regulatory arbitrage, but they illustrate different philosophies on how to enable NBFIs competition while crafting a risk-sensitive prudential perimeter.

Note: A crore is equal to 10 million (10,000,000) rupees.

It is worth noting that while India and Brazil are cited as illustrative cases of jurisdictions applying scale-based or proportional regulation for NBFIs or small banking entities, the drivers and institutional constraints in their deposit and lending markets reflect the institutional contexts of each market as well as the development of NBFIs participation, which may help account for each jurisdiction's prudential design choices. Source: Ehrentraud, J; Mure, S; Noble, E; Zamil, R (2024), Safeguarding the financial system's spare tyre: regulating non-bank retail lenders in the digital era, <https://www.bis.org/fsi/publ/insights56.pdf>; Central Bank of Brazil (2025), Financial Stability Regulation, <https://www.bcb.gov.br/en/financialstability/regulation>; Reserve Bank of India (2023), Master Direction – Reserve Bank of India (Non-Banking Financial Company– Scale Based Regulation) Directions, https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12550.

3.1.2. Enabling exit

84. Contestable banking markets require not only the potential for entry, but also the possibility of credible exit (Vives, 2016^[4]). Competition ensures that inefficient institutions can lose market share and, if necessary, exit the market. By contrast, inefficient prudential regulation and supervision may prop up underperforming banks, distorting market outcomes and weakening stability (OECD, 2017^[3]). Where exit is delayed or obstructed, inefficient banks may continue to absorb resources, depress consumer outcomes, and undermine the incentives and ability for well-managed competitors to expand. Prudential authorities, thus, play a vital role in ensuring that exit is feasible without compromising stability.

85. Since the global financial crisis, new resolution mechanisms have been introduced across jurisdictions to manage bank failures in an orderly way. These frameworks, ranging from “living wills” to bail-in instruments, are designed to prevent contagion, protect critical functions and reduce the need for taxpayer-funded bailouts. By enabling “safe” exit, they reduce the risk that inefficient or poorly managed institutions remain in the market solely because they are perceived as TBTF.

86. Importantly, while resolution regimes can be organised differently and take different forms, the Financial Stability Board has published key attributes of effective resolution regimes for financial institutions to inform their effective implementation. The FSB key attributes set out high-level standards for resolution authorities, defining resolution as an administrative process conducted in pursuit of public interest objectives

by an authority equipped with the mandate, powers and operational capacity to act effectively. This principle underpins the key attributes, while leaving jurisdictions' flexibility in the institutional design of their resolution frameworks (FSB, 2024^[85]).

87. For example, a living will, also known as a recovery and resolution plan, is a document that large or systemically important financial institutions are required to prepare, setting out how they can be resolved in an orderly way if they fail. In the US, under the Dodd–Frank Act, systemically important financial institutions are required to submit living wills to the Federal Reserve and the Federal Deposit Insurance Corporation. In the EU, the Bank Recovery and Resolution Directive requires banks to prepare recovery and resolution plans in a similar manner (Baudino, Sánchez and Walters, 2021^[86]).

88. A key innovation in resolution regimes is the use of bail-ins. Where bailouts involve the use of public funds to recapitalise failing banks, which may preserve short-term stability but risks encouraging moral hazard and reinforcing the funding advantages of large incumbents, bail-ins allow resolution authorities to impose requirements upfront. Because bail-ins shift the burden of failure away from taxpayers, they may avoid moral hazard and have the potential to help prevent inefficient banks from surviving based on implicit state support (Baudino, Sánchez and Walters, 2021^[86]).

89. From a competition perspective, effective resolution supports contestability. It ensures that unprofitable and failing institutions can be restructured or wound down without permanently increasing concentration. It also lowers the risk of distortive state aid or ad hoc support that insulates incumbents, while rivals must compete without such guarantees. In recent years, prudential and competition authorities have converged on the view that inefficient large institutions simultaneously undermine both financial stability and competition (Cœuré, 2025^[15]). Resolution frameworks can therefore be seen as pro-competitive prudential instruments. By making credible the possibility of exit, they mitigate the moral hazard that fuels excessive risk-taking and TBTF distortions. They also reassure markets that losses will be absorbed by shareholders and creditors, rather than by taxpayers, thereby limiting implicit subsidies that would otherwise give large incumbents an undue funding advantage. In turn, smaller or more efficient competitors can expand without facing the uneven playing field created by expectations of state support.

90. Resolution mechanisms complement competition enforcement. Extraordinary mergers used as resolution tools, for example, when a healthy bank acquires a failing competitor, may create lasting concentration risks if not scrutinised carefully, as discussed in Section 3.2.2. Close co-ordination between prudential regulators and competition authorities is therefore helpful: prudential tools can secure stability in the short term, while competition enforcement ensures that banking markets remain contestable in the long term.

3.1.3. Considerations for licensing and capital requirements

91. The analysis in Section 2.1 discusses certain prudential requirements that can play a central role in shaping entry and expansion conditions in retail banking and lending markets. While these requirements are crucial to safeguard stability, they may also unintentionally create competition bottlenecks if they are disproportionate to risks, fail to accommodate new business models, or do not consider the effects on entry and expansion incentives or abilities. This Section highlights certain considerations relevant to their potential proportionality, simplicity and flexibility, which may be relevant to prudential design, particularly where competition is observed to be weak.

92. First, capital requirements can function both as essential prudential safeguards and as a potential unintended competition bottleneck. When setting capital requirements, authorities might benefit from establishing standards based on international experiences with similar services or entities to ensure that minimum requirements are not set too high or imposed unnecessarily (OECD, 2023^[58]).

93. Moreover, when capital requirements are applied through overly complex or unevenly calibrated methodologies, capital frameworks may unintentionally entrench incumbents' advantages and

disadvantage smaller or newer entrants. For example, under the advanced internal ratings-based approach, banks use their own internal risk models to calculate required capital. This may result in lower effective risk weights for comparable exposures compared to the standardised approach, which is applied to smaller or less complex institutions using supervisor-set parameters. This divergence, driven by differences in modelling sophistication rather than underlying risk, may affect competition where it exists.

94. The Basel Committee's emphasis on proportionality allows scope for tailoring requirements without undermining stability. Policymakers can deploy tiered capital regimes that impose stricter standards on systemically important banks while permitting smaller, less risky institutions to operate under simpler, less burdensome rules (BCBS, 2025^[59]). Well-calibrated capital frameworks can simultaneously maintain resilience while ensuring that incumbents do not enjoy structural advantages solely due to scale or sophistication. Box 12 discusses experiences across several jurisdictions regarding balancing capital requirements with competition considerations.

Box 12. Calibrating capital requirements

New Zealand

In New Zealand, the Commerce Commission's 2024 competition report on personal banking services found that regulatory requirements impose substantial fixed costs on market participation, limiting the ability of smaller banks and NBFIs to compete when they lack the scale of major banks. As such, proportionality in regulatory policy settings was identified as key to increasing competition. In particular, capital requirements were identified as one of the prudential regulatory conditions affecting entry and expansion in retail banking services. Prior to the Reserve Bank's Capital Review in 2022, capital requirements were found to have given major banks a competitive advantage over smaller banks and NBFIs. By 2024, the changes made through the Capital Review had reduced, but not eliminated, this competitive advantage to major banks. The remaining differential was identified as due to differences in internal risk-based modelling outcomes and those under the standardised approaches.

That is, between 2008 and 2022, prudential capital settings allowed the four major banks to hold materially less capital than smaller banks for assets with the same or similar risks. This gave the major banks a competitive advantage while restricting smaller banks' ability to compete. Particularly, as they had less capital available for growth, innovation and investment. The Reserve Bank's 2019 capital review aimed to implement changes to eliminate those differences following the initial implementation in 2022. However, the smaller banks disputed that those differences had been eliminated after 2022. The Commerce Commission's report underscored that while these advantages to the incumbents had been reduced, they had not been eliminated.

The Deposit Takers Act 2023, which requires the Reserve Bank to develop new prudential standards and develop a framework for considering proportionality principles and competition, provided an opportunity to recalibrate capital requirements with competition in mind. Indeed, at the time of the Commerce Commission's 2024 competition report, the Reserve Bank was already consulting on capital requirements for the Deposit Takers Act 2023. The Reserve Bank did not propose changing the "1-in-200-year risk" setting that it had applied in the Capital Review. It did, however, propose lowering the minimum capital requirements for licensed banks and non-bank deposit takers. A Select Committee Inquiry into banking competition and further industry challenge to the "1-in-200-year risk" setting prompted the Reserve Bank to announce a further review of its capital settings, to be completed by the end of 2025.

In this connection, while the Commerce Commission's competition report on personal banking services did not recommend reviewing the Reserve Bank's "1-in-200-year risk" settings, as the settings applied

across the market. It did, however, recommend that the Reserve Bank broaden its competition assessments and place greater focus on reducing barriers to the entry or expansion of smaller providers, including by refining standardised risk-weightings for capital ratios. In particular, it suggested that the Reserve Bank consider whether standardised risk-weighting could be refined to enable entry and expansion by permitting smaller providers to use more granular standardised risk weightings. This would allow smaller providers to more closely match the risk weightings to the actual risks their loans create and thus potentially reduce the capital they need to hold. The Commerce Commission also made recommendations regarding New Zealand's deposit guarantee scheme, which are discussed further in Box 14.

Australia

The Australian Competition and Consumer Commission's 2023 retail deposits inquiry highlighted concerns that capital requirements can provide competitive advantages, similar to those observed in New Zealand. Notably, the inquiry found that capital requirements set using the advanced approach, also known as the internal ratings-based approach, which allows banks to use their internal risk models for calculation, tend to be lower. That is, as opposed to the standardised approach, which applies a common prescribed standard by the prudential supervisor. Major banks generally use the advanced approach rather than the standardised approach. Importantly, however, it also found that the difference in approaches has been mitigated by the new capital framework implemented by the prudential supervisor. This framework increases minimum capital requirements for banks using the advanced approach and reduces capital requirements for banks using the standardised approach.

United Kingdom

The UK's "Strong and Simple" framework, discussed in Box 8, extends to the capital framework, which aims to significantly simplify the capital requirements for small domestic deposit-takers in the UK, while maintaining their resilience. Namely, by using simpler risk-weighted asset calculations, the regime is designed to foster a more competitive banking sector. In assessing the proposals, the PRA considered that the regime would lead to lower costs for institutions due to simplified compliance with prudential regulation, potentially increasing the incentives for small foreign banks to establish branches in the UK. The simplification regime will take effect in January 2027. Therefore, it will be interesting to monitor whether and to what extent the framework benefits competition in the future

Notes: "1-in-200-year risk" settings refer to capital requirements that each company must hold to withstand 199 adverse risk events out of the next 200 years. Many jurisdictions set their capital requirements to a "1-in-100-year risk," that is, to withstand 99 adverse risk events over the next 100 years.

The UK's proposals differ from some Basel standards. However, given that those standards are designed to apply to internationally active banks, whereas small domestic deposit-takers are domestic, the UK continues to align with Basel standards.

Source: Commerce Commission New Zealand (2024), Personal banking services final competition report, https://comcom.govt.nz/data/assets/pdf_file/0019/362035/Final-report-Personal-banking-services-market-study-20-August-2024-Amended-27-August-2024.pdf; Reserve Bank of New Zealand (2025), 2025 Review of key capital settings, https://consultations.rbnz.govt.nz/prudential-policy/review-of-key-capital-settings/user_uploads/consultation-paper-review-of-key-capital-settings.pdf; Reserve Bank of New Zealand (2025), 2025 Review of key capital settings, <https://www.rbnz.govt.nz/regulation-and-supervision/oversight-of-banks/how-we-regulate-and-supervise-banks/our-policy-work-for-bank-oversight/2025-review-of-key-capital-settings>; Australian Competition and Consumer Commission (2023), Retail deposits inquiry - Final report, <https://www.accc.gov.au/system/files/Retail-deposits-inquiry-final-report.pdf>; Bank of England (2023), Operating the Small Domestic Deposit Taker (SDDT) regime, <https://www.bankofengland.co.uk/prudential-regulation/publication/2023/december/small-domestic-deposit-taker-regime>; Bank of England (2024), The Strong and Simple Framework: The simplified capital regime for Small Domestic Deposit Takers (SDDTs), <https://www.bankofengland.co.uk/prudential-regulation/publication/2024/september/strong-and-simple-framework-the-simplified-capital-regime-for-sddts-cp>.

95. Second, where competition is observed to be weak, a potential consideration to stimulate entry and expansion may be whether to extend the scope of permissible activities. For instance, by allowing NBFIs to accept certain types of less-risky deposits (e.g., term deposits) while subjecting them to prudential

safeguards. For example, though exceptional, several jurisdictions permit NBFIs to take term deposits, subject to prudential conditions (see Table 2.1).

96. The Basel Core Principles for Effective Banking Supervision emphasise that accepting deposits should be limited to institutions that hold a banking license or are subject to supervision as banks (BCBS, 2024^[87]). However, the same Core Principles note that when NBFIs are allowed to accept deposits under different regulations than banks, these institutions should be subject to a regulatory framework appropriate to the nature and scale of their operations (BCBS, 2024^[87]). Thus, in accordance with the Basel Core Principles, some jurisdictions permit certain non-bank entities to accept term deposits without being subject to the same level of supervision as banks (Ehrentraud et al., 2024^[53]).

97. Particularly, because time deposits have contractual maturities, they may help institutions better manage liquidity outflows and pose lower risks than demand deposits. Where such activities are permitted to NBFIs, competitive neutrality principles can help inform the calibration of accompanying prudential obligations (e.g., capital requirements or deposit-guarantee schemes).⁴¹ Design choices, therefore, involve a balancing exercise: opening limited deposit-taking may improve contestability and consumer choice, while proportionate safeguards, such as risk-based capital requirements, large exposure limits, creditworthiness assessments, fit and proper management assessments and supervisory reporting, can help preserve stability (Ehrentraud et al., 2024^[53]). A potential benefit of allowing term deposit-taking by NBFIs, which are subject to appropriate oversight, is that it provides pathways to expansion and alternative entry routes, reducing dependence on bank partnerships. Box 13 provides an example from Mexico.

Box 13. Mexico's NBFi tiered licensing structure

NBFIs in Mexico have benefited from a tiered licensing framework that aligns regulatory requirements with business models and risk profiles. For instance, NBFIs may extend credit without a license, provided they do not take deposits. To mobilise deposits, NBFIs can apply for a Sociedad Financiera Popular (SOFIPO) licence, which allows them to accept retail deposits while imposing prudential obligations, including participation in a deposit guarantee scheme. This structure enables proportionate supervision and entry into deposit-taking without requiring a full banking charter. Although SOFIPO licenses were introduced primarily to promote financial inclusion, they have also enhanced competition by lowering barriers to entry and facilitating a gradual path toward full authorisation.

Several market participants have made use of this framework to expand their activities gradually.

Nubank, initially launched in Mexico in 2020 as an unregulated lender, entered the market with a no-fee credit card product. As its lending portfolio grew, it expanded into payments and later deposits under a Sociedad Financiera Popular licence obtained in 2022. The SOFIPO framework allowed Nubank to mobilise deposits with proportionate prudential requirements and deposit insurance, maintaining consumer confidence without the regulatory burden of a full bank charter. In April 2025, Nubank obtained a full banking licence, reflecting both its growth trajectory and the supervisory pathway designed to align prudential obligations with institutional scale and complexity.

Klar, another prominent FinTech lender, followed a similar incremental licensing path. Founded in 2019, Klar began by offering unsecured consumer credit through partnerships with licensed financial institutions. Over time, Klar obtained its own Sociedad Financiera Popular licence, enabling it to intermediate deposits directly and expand into digital savings products. The firm's growth trajectory demonstrates how proportional regulation can facilitate the scaling of domestic entrants, allowing them to compete with incumbents while maintaining prudential safeguards. Klar's 2024 announcement of profitability and plans to pursue a full banking licence underscore the role of the SOFIPO model as a stepping stone from non-bank intermediation to fully regulated banking.

Stori, launched in 2018, initially operated under the non-bank credit provider model, offering credit cards to previously unbanked consumers. After securing significant investment, Stori obtained a SOFIPO licence in 2023, allowing it to mobilise deposits and diversify its funding base. Like Klar, Stori's transition from pure lending to deposit intermediation reflects the ability of Mexico's licensing framework to accommodate FinTech evolution within a prudentially proportionate regime. The move also aligns with financial inclusion objectives, as Stori serves a large base of first-time borrowers and depositors who were previously excluded from formal credit markets.

Taken together, these cases highlight how Mexico's graduated prudential perimeter supports entry and scaling while maintaining stability. By providing multiple licensing tiers (from unlicensed credit provision to SOFIPO status and, ultimately, full bank authorisation), the framework allows supervision to evolve in line with institutional growth and systemic importance. The entry of digital lenders such as Nubank, Klar and Stori has broadened access to credit and contributed to lower borrowing costs in certain market segments. According to the Bank of Mexico, average credit card interest rates offered by new entrants are several percentage points lower than those of traditional banks, while savings accounts introduced by SOFIPOs have increased average yields offered to small depositors.

Source: Cofece (2024), Study of Competition and Free Market Access in Digital Financial Services, https://www.cofece.mx/wp-content/uploads/2024/11/EE24-F_fintech-ENG_1DEAI-1-1.pdf; Barakova, I., J. Ehrentraud and L. Leposke (2024), A two-sided affair: banks and tech firms in banking, <https://www.bis.org/fsi/publ/insights60.htm>; Nubank (2025), Nu Mexico receives banking license approval, paving the way for product portfolio expansion and increased financial inclusion, <https://international.nubank.com.br/company/nu-mexico-receives-banking-license-approval-paving-the-way-for-product-portfolio-expansion-and-increased-financial-inclusion/>; Mexican Government (2016), Sociedades Financieras Populares, Sociedades Financieras Comunitarias, <https://www.gob.mx/cnbv/acciones-y-programas/sociedades-financieras-populares-sociedades-financieras-comunitarias>; Mexico Financial License (2025), Mexico Licensing Guide 2025, <https://mexicofinanciallicense.com/wp-content/uploads/2025/08/Mexico-Licensing-Guide-2025.pdf>; Klar (2025), Klar Aims for Bank License Amid Growing Financial Inclusion, <https://mex.news.o-abroad.com/~economy/169751-en-klar-aims-for-bank-license-amid-growing-financial-inclusion.html>; Bloomberg (2025), Fintech Klar catches up on race to bank status with purchase, <https://www.bloomberg.com/news/articles/2025-09-05/fintech-klar-catches-up-on-race-to-bank-license-with-purchase-of-banorte-s-bineo>; Newswire (2023), Stori, the Mexican Unicorn, obtains approval to acquire the Sofipo MasCaja, a licensed deposit entity, to expand its product offering, <https://www.prnewswire.com/news-releases/stori-the-mexican-unicorn-obtains-approval-to-acquire-the-sofipo-mascaja-a-licensed-deposit-entity-to-expand-its-product-offering-301921035.html>; Finextra (2024), Mexican fintech Stori raises \$212 million, <https://www.finextra.com/newsarticle/44557/mexican-fintech-stori-raises-212-million>; Banco de Mexico (2024), Financial Stability Report, <https://www.banxico.org.mx/publications-and-press/financial-system-reports/%7B1DDCC744-D56B-0BA1-584B-52DAADCA217E%7D.pdf>.

98. Relatedly, deposit guarantee schemes may consider avoiding one-size-fits-all funding models that may impose disproportionate burdens on small challengers. That is, they may benefit from preserving incentives for prudential risk management while assessing contributions to each institution's size, complexity, or risk profile. Moreover, perimeter choices generally may benefit from considering their impact across multiple policy spheres, including competition. As further discussed in Section 3.3, competition assessments of regulations can be a helpful tool when undertaking this balancing act.⁴² Box 14 provides an example from New Zealand.

Box 14. New Zealand's deposit guarantee scheme

New Zealand is an example of balancing prudential and competition considerations in assessing whether the regulatory perimeter applicable to NBFIs should be extended to include deposit insurance. New Zealand allows NBFIs to hold term deposits. Under the Non-Bank Deposit Takers Act 2013, NBFIs were subject to a prudential framework. However, in the context of the Deposit Takers Act 2023, which aims to modernise New Zealand's regulatory framework for both banks and NBFIs, the government assessed whether (i) to extend deposit insurance to NBFIs deposit-takers, or to exclude them and (ii) in what proportion levies should be imposed.

In assessing whether to bring NBFIs into the deposit insurance fold, the government conducted a regulatory impact assessment in 2024 on the proposed depositor compensation scheme (DCS)

regulations, which considered the potential impact on prudential and competition objectives. In this assessment, the government found that deposit insurance would change the risk profile of most risk-takers, benefiting prudential objectives. At the same time, it asserted that it would “place pressure on deposit rates and increase competition in the deposit-taking market, by increasing the sensitivity depositors have to the interest rates they are offered (increase in price elasticity).”

Notably, however, the Commerce Commission’s competition report on personal banking services, also from 2024, recommended that the Reserve Bank “broaden its competition assessment and place greater focus on reducing barriers to entry or expansion for smaller providers.” It also advised the government to “err on the side of not adding to the burden on small deposit takers until more is known on the impacts of introducing the DCS, including relative to costs different deposit takers will impose on the scheme.”

Regarding how levies should be imposed, major banks argued that levies should be risk-based to ensure that providers most likely to fail pay more, thereby avoiding unjustified risk-taking and cross-subsidisation of riskier providers. Smaller banks and NBFIs, in turn, argued that a fully risk-based levy would be potentially unaffordable for some of them and potentially place a disproportionately higher burden on them to meet. The Commerce Commission recommended an initial flat-rate levy until more is known of the impacts of introducing the DCS.

Ultimately, deposit-taking NBFIs were required to participate in deposit guarantee schemes applicable to them. The DCS came into effect in July 2025, fully funded by industry participant levies. The levies imposed on institutions for the safety net are based on each institution's size and risk assessment. Credit unions and building societies will, however, pay a flat-based levy, meaning their levy will be set in proportion to their estimated covered deposits. In 2028, when the Deposit Takers Act is fully in force, the risk-based levy will apply to all deposit takers. The Finance Ministry underscored that “[t]he levy will be based on total deposits covered by the scheme, so the four largest banks will pay about three quarters of the total.” Additional considerations include, for example, the likelihood of needing to draw on the deposit guarantee payout and the impact of the levy on entity soundness.

Moreover, in response to the Commerce Commission’s recommendations, the Finance Minister has stated that, while the DCS is expected to improve competition in the sector, the scheme's impact will be monitored. As of this writing, the DCS's effects on consumer behaviours and competition for deposits, as well as whether the DCS has enabled smaller deposit-takers to attract more deposits than previously, remain to be seen. Thus, it will remain important to monitor the perimeter choice and the proportionality of the levies and their impact on competition going forward.

Note: In New Zealand, high bank profitability and concentration (compared to international comparisons) identified a lack of competition in the banking industry and led to multiple reviews of the sector by relevant agencies, including the Commerce Commission, at the direction of the Government, to revamp competition.

Source: Reserve Bank of New Zealand (2024) Regulatory Impact Statement: Depositor Compensation Scheme Regulation, <https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/proactive-releases/2024/regulatory-impact-statement-dcs-regulations-2024.pdf>; Reserve Bank of New Zealand (2024), Depositor Compensation Scheme - Transitional Advice, <https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/about/our-legislation/depositor-compensation-scheme-transitional-advice-rbnz-6118.pdf>; Reserve Bank of New Zealand (2024), Depositor Compensation Scheme levy approach agreed, <https://www.rbnz.govt.nz/regulation-and-supervision/deposit-takers-act/dcs-levy-approach-agreed>; Reserve Bank of New Zealand (2025), Reserve Bank of New Zealand (2023), Overview of the Deposit Takers Act, <https://www.rbnz.govt.nz/regulation-and-supervision/deposit-takers-act/overview-dta>; Commerce Commission New Zealand (2024), Personal banking services final competition report, https://comcom.govt.nz/_data/assets/pdf_file/0019/362035/Final-report-Personal-banking-services-market-study-20-August-2024-Amended-27-August-2024.pdf; Savage, K (2024), A risk-based funding model for the new depositor compensation scheme will see the four largest banks bear most of the cost of the safety net with smaller entities subject initially to a flat fee, Good Returns, <https://www.goodreturns.co.nz/article/976523786/govt-takes-risk-based-approach-to-deposit-guarantee-scheme.html>; Reserve Bank of New Zealand (2025), Depositor Compensation Scheme now in effect; <https://www.rbnz.govt.nz/hub/news/2025/07/depositor-compensation-scheme-now-in-effect>; Ehrentraud, J; Mure, S; Noble, E; Zamil, R (2024), Safeguarding the financial system’s spare tyre: regulating non-bank retail lenders in the digital era, <https://www.bis.org/fsi/publ/insights56.pdf>; Dennerly, C. (2024), Revamping competition in New Zealand, OECD Economics Department Working Papers, No. 1817, OECD Publishing, Paris, <https://doi.org/10.1787/8bbb404-en>.

99. Third, certain jurisdictions have also promoted competition by adopting a more flexible approach to licensing and supervisory requirements for digital business models based on risk. As discussed in Section 2.1.1, licensing regimes can create barriers for digital or cross-border entrants when requirements, such as local presence obligations, particularly physical branch requirements, are not well aligned with technology-driven or cross-border business models. In response, some jurisdictions have recalibrated their frameworks to balance innovation, prudential oversight and market contestability. Box 15 discusses Hong Kong's (China) experience with digital-only bank licenses.

Box 15. Digital-only bank licenses in Hong Kong (China)

In addition to enabling NBFIs to hold term deposits, as illustrated in Table 2.1, the government has facilitated the introduction of digital banks by creating digital-only bank licenses and releasing accompanying Guidance in 2018. These licenses cater to the unique characteristics of digital banks by adapting supervisory requirements to their business models, using a risk-based, technology-neutral approach. For example, digital-only licenses do not include local presence obligations such as a physical branch or minimum in-country staffing, but instead require local incorporation, governance and operational oversight. In its 2024 review of virtual banks, the Monetary Authority concluded that the development of virtual banking positively impacted competition in the overall banking sector, with incumbent banks responding to competitive pressure from new entrants.

Note: Importantly, in the context of the 2024 review of banks, the Monetary Authority expressed concern that not all eight of the current digital-only banks are yet profitable. The authority is thus hesitant toward granting more digital-only licenses. In this context, as the market evolves, it may be worthwhile to consider the positive effects of perceived or actual potential competition enabled by the possibility of market entry. Market participants' innovative incentives may weaken if there is no perception of an ongoing threat from new challengers. Moreover, alternatives to address profitability and thus the resilience of the sector may include enabling exit mechanisms for less efficient competitors. Source: HKMA (2025), Digital Banks, <https://www.hkma.gov.hk/eng/key-functions/banking/banking-regulatory-and-supervisory-regime/digital-banks/>; HKMA (2024), Report on the review of virtual banks, <https://www.hkma.gov.hk/media/eng/doc/key-information/press-release/2024/20240806e3a1.pdf>.

3.2. Examples of how competition may support prudential objectives

3.2.1. Interest rates

100. Multiple recent market studies across jurisdictions underscore that concentrated market structures, combined with the structural barriers present in deposit and lending markets, are associated with slower, weaker and more selective pass-through of savings and lending rates to consumers.⁴³ Legislators have also expressed concerns about this weak pass-through. In the UK, for example, recent parliamentary debates noted that “[h]igher interest rates have not been passed on to savers; they have been hoarded by the banks, creating a windfall for them of many billions for doing nothing productive” (UK Parliament, 2023_[68]).

101. This perception has led to the adoption of windfall taxes on banks in many jurisdictions. Such taxes may have fiscal and redistributive objectives, such as raising funds to invest in public services.⁴⁴ Competition enforcement and competition-enabling policy tools, under appropriate prudential safeguards, offer an alternative or complementary approach that directly targets the lack of competitive pressure on incumbent banks, which leads to weak pass-through.

102. For example, the introduction of competition-enabling tools can address structural and behavioural frictions that weaken pass-through. Market studies in Australia, Belgium and New Zealand converge on the importance of improving transparency, comparability and switching.⁴⁵ For instance, the ACCC recommended reforms to improve consumer awareness of deposit rates and to facilitate easier comparison across banks (ACCC, 2023_[40]). The Belgian Competition Authority called for simplifying or removing the dual-rate system of base and loyalty bonuses, which makes savings products less transparent and less

comparable (BCA, 2023^[21]). New Zealand's Commerce Commission placed particular emphasis on implementing open banking and strengthening the role of challenger providers (ComCom, 2024^[41]). Each of these recommendations recognises that by lowering switching costs and reducing information asymmetries, regulators can spur greater customer mobility and competitive pressure, ultimately increasing the responsiveness of banks to interest rate changes.

103. Historical international experiences also suggest that enabling competition can be a more durable solution than fiscal interventions such as windfall taxes (Dell'Ariccia, 2001^[89]; Van Leuvensteijn et al., 2008^[50]).⁴⁶ Initiatives that promote entry, empower challengers and facilitate customer switching not only enhance pass-through in deposit markets but also improve access to credit. Improved access to credit may not only lower borrowing costs but also reduce borrower defaults and system risk (OECD, 2017^[10]).

104. In other words, strengthening interest-rate pass-through can also advance prudential objectives by improving the transmission of monetary policy and the quality of bank loan portfolios. As discussed in Section 1.3, one of the channels through which monetary policy affects the real economy is the credit channel, with monetary easing influencing the cost and availability of bank credit (Byrne and Kelly, 2017^[49]). When declines in policy rates are only partially reflected in lending rates, borrowing costs remain elevated relative to funding costs, heightening repayment pressures and credit risk, particularly among highly leveraged households and SMEs. Persistently high lending spreads can erode loan performance and weaken banks' balance-sheet resilience. By contrast, more contestable and transparent lending markets may foster quicker and more even rate adjustment, aligning borrowing costs more closely with monetary policy conditions and mitigating the build-up of credit risk (Byrne and Kelly, 2017^[49]; Van Leuvensteijn et al., 2008^[50]). At the same time, enhanced competition can compress interest margins and incentivise risk-taking by banks. Thus, adequate prudential oversight, as a complement to competition, remains important to prevent excessive risk-taking (Vives, 2016^[4]; Byrne and Kelly, 2017^[49]; Van Leuvensteijn et al., 2008^[50]). Under such safeguards, competition can reinforce effective transmission while supporting overall financial stability.

3.2.2. Merger enforcement and competitive neutrality

105. As discussed in Section 2.2, merger control is central to ensuring that long-lasting anticompetitive effects from concentration do not materialise. By curbing excessive concentration and preserving diversity in ownership and business models, merger enforcement can mitigate risk and strengthen the resilience of the financial system. In this way, effective merger control can complement prudential objectives by promoting a more diversified and contestable banking sector. Competitive and well-diversified financial systems are likely to be less prone to systemic risk and better able to absorb shocks (OECD, 2017^[3]; 2011^[2]). Merger control, together with prudential tools such as resolution regimes, can therefore enhance stability. Sustained co-ordination between prudential regulators and competition authorities helps align short-term crisis management with long-term market resilience. Relaxing merger control on stability grounds, by contrast, can entrench incumbents, distort incentives and magnify TBTF risks.

106. Experience from past crises shows that stability considerations have at times outweighed competition concerns, even where subsequent evidence indicated that consolidation weakened long-term performance and innovation (Vickers, 2010^[90]; OECD, 2011^[2]; Philippon, 2017^[52]). The failing-firm defence, recognised in most jurisdictions by competition authorities as a narrowly drawn exception, applies to the review of mergers where the risk of a failing firm exiting the market is present. Where used cautiously, this mechanism can balance stability and competition, but over-reliance on it risks normalising concentration. In addition, prudential resolution instruments, such as bail-ins, living-wills and recovery planning, provide credible alternatives to anti-competitive combinations, safeguarding financial stability without undermining market entry and rivalry.

107. Moreover, maintaining competitive neutrality in the treatment of market participants and avoiding preferential support or implicit guarantees that encourage risk-taking reinforces market discipline and

reduces the consequences of moral hazard. A level playing field helps ensure that financial institutions compete on the basis of efficiency and sound risk management rather than implicit support. Competitive neutrality, therefore, can contribute to stable financial intermediation by discouraging excessive risk-taking and fostering trust in the system as a whole. In sum, ensuring neutrality in public support frameworks can provide an important complement to prudential and competition objectives.

108. Box 16 discusses lessons from Korea, underscoring why the benefits of competition should not be overlooked in the context of financial stability.

Box 16. Korea: competition and financial stability

In Korea, both weak competition enforcement and prudential oversight have been found to have contributed to the 1997 financial crisis. Limited enforcement, combined with weak corporate governance and prudential oversight, allowed conglomerates to expand through excessive leverage and inefficient investment, distorting incentives and masking losses until the system's eventual collapse.

Before the crisis, during earlier periods of economic stress, various crisis-motivated cartels were permitted under Korean law. The Price Stabilisation and Fair Trade Act of 1975 aimed primarily to control inflation and stabilise markets by co-ordinating prices and output across industries. As a result, competition considerations were subordinated to short-term stability objectives, with numerous government-approved "rationalisation" or "depression" cartels operating during that period.

Two key lessons emerged from the 1997 financial crisis that remain relevant to current assessments on the balance between stability and competition. First, during crises, government agencies may overlook the beneficial effects of competition, prioritising short-term stabilisation over longer-term market resilience. The Korean experience has since demonstrated that vigorous competition enforcement, even in times of economic stress, can help ensure that emergency measures do not unnecessarily distort market structure or entrench incumbents.

Second, the Korean authorities have also emphasised that, in line with principles of competitive neutrality, even in crises, the least anti-competitive solutions should always be sought. In sum, as exhibited by Korea since the 1997 crisis, promoting competition can restore market confidence and lay the foundations for sustainable economic recovery. In the wake of the global financial crisis and more recently, the Korean government reaffirmed this approach, underscoring the importance of competition enforcement in the recovery process.

Source: OECD (2011), *Competition Issues in the Financial Sector: Key Findings*, OECD Publishing, Paris, <https://doi.org/10.1787/37dd5552-en>; Lee, W, KFTC vows to tackle cartels, unfair trade, amid political, economic uncertainty, <https://www.mlex.com/mlex/articles/2280994/kftc-vows-to-tackle-cartels-unfair-trade-amid-political-economic-uncertainty>; OECD (2021), Regulatory quality and competition policy in Korea, https://www.oecd.org/en/publications/korean-focus-areas_f91f3b75-en/regulatory-quality-and-competition-policy-in-korea_e5b4137d-en.html; Coe, T; Kim, S (2002), What Have We Learned from the Korean Economic Adjustment Program?, <https://www.elibrary.imf.org/display/book/9781589060685/C03.xml>; OECD (2021), Korea and the OECD: 25 years and beyond, <https://www.oecd.org/content/dam/oecd/en/about/projects/edu/education-policy-outlook/Korea%20and%20the%20OECD.pdf>; Lee, H (2015), Development of Competition Laws in Korea, <https://www.eria.org/ERIA-DP-2015-78.pdf>; OECD (2011), Crisis Cartels : Key findings, summary and notes, *OECD Roundtables on Competition Policy Papers*, No. 119, OECD Publishing, Paris, <https://doi.org/10.1787/39a0d2e8-en>.

3.3. Considerations for enhanced co-operation

109. Prudential and competition authorities pursue distinct objectives; however, their policy choices intersect in practice. Decisions on licensing, capital, resolution, and supervision inevitably shape market structure, entry conditions, and incentives, just as competition outcomes can influence prudential

resilience. Ensuring that these interactions remain neutral or mutually reinforcing benefits from ongoing co-operation. The following discussion highlights areas where co-ordination may be particularly valuable, as well as tools that may help align stability and competition objectives.

110. One area where co-operation can be especially critical is in enabling the orderly exit of inefficient institutions through resolution mechanisms. Such frameworks can help avoid crisis-driven mergers or bailouts. Rather than relying on consolidation, state support, or intervention to preserve short-term stability, well-designed resolution regimes can support better long-term outcomes by preventing further concentration, entrenchment, or the reinforcement of TBTF structures. Absent co-ordination, crisis measures risk creating lasting market distortions that are costly to unwind. Structured dialogue, however, allows prudential authorities to shape resolution frameworks in advance, benefiting from competition perspectives. This enables orderly exits without contagion and aligns stability and competition objectives.

111. Similarly, competition authorities can help guide proportionate considerations, preserving a level playing field for smaller entrants while maintaining prudential safeguards. Particularly, systematic competition impact assessments of new and existing laws or regulations, using instruments such as the OECD Competition Assessment Recommendation and Toolkit, can help operationalise complementarities and co-operation by identifying and amending rules that unintentionally or unnecessarily restrict competition and balance prudential goals (OECD, 2019^[91]). Additionally, the OECD Recommendation on Competitive Neutrality and Toolkit provides competition authorities and other public officials with tools to identify government policies that may distort the level playing field and to develop alternatives that minimise such distortions (OECD, 2024^[81]). Moreover, proportionality mechanisms that scale prudential requirements to firms' complexity or risk profiles, preventing disproportionate burdens on smaller providers, along with the simplification of rules, may also be helpful guiding principles for balancing. This can help ensure that obligations are clear for smaller players to comply with and for supervisors to enforce.⁴⁷

112. Another area for co-operation across authorities lies in joint market monitoring and forward-looking assessments, including through joint committees or frequent exchanges. In line with, or as part of, competition impact assessments, they can help identify unintended anticompetitive effects of prudential measures. Regular market studies and horizon scanning can also help identify current and potential future vulnerabilities and trade-offs. For example, in Israel, an Interministerial Committee was created this year to advance banking competition. The committee includes participation from the Competition Authority, the Central Bank and the Finance Ministry, amongst others. Their focus will be on removing restrictions to competition and lowering entry barriers for new participants, including NBFIs (Bank of Israel, 2025^[92]).

113. Furthermore, regulatory sandboxes allow new entrants to test services under supervision, giving regulators early insights into risks while lowering entry barriers for smaller or non-traditional providers (World Bank, 2020^[93]). For example, in Spain, following the CNMC's market study on the impact of new financial technologies and its recommendation to create a regulatory sandbox to support innovation without heavy entry barriers, the Spanish Parliament adopted the sandbox proposal (CNMC, 2018^[94]) (Government of Spain, 2020^[95]). Cross-border sandbox initiatives can further reduce duplicative compliance costs, prevent regulatory arbitrage and promote consistent standards across jurisdictions, which may help fuel new entry and enhance competition. By providing a controlled space for experimentation, sandboxes can help prudential and competition authorities, including across jurisdictions, calibrate proportionate rules while supporting innovation and contestability (World Bank, 2020^[93]).

114. Co-operation can range from informal exchanges to more formalised arrangements with defined procedures for consultation. Examples from practice show that institutionalised co-operation is valuable. In Portugal, the competition authority and the Bank of Portugal have built mechanisms for sustained collaboration across advocacy, supervision and enforcement. This allows each authority to act within its mandate while reinforcing the other's objectives (OECD, 2025^[96]). In the UK, concurrent powers between financial and competition regulators, alongside forums such as the Digital Regulation Co-operation Forum,

have fostered joint assessments and shared regulatory messaging (OECD, 2025^[97]). Yet, co-operation does not necessarily need to be formalised. What matters is that regular communication ensures both perspectives are reflected in decision-making. Whether through memoranda of understanding or informal dialogue, clear mandates and sustained engagement can help avoid tensions, reduce gaps and ensure coherent enforcement.

115. The cross-border dimension to the provision of financial services reinforces the benefits of international co-operation. Openness to foreign bank entry, with fewer restrictions on activities subject to strong safeguards and oversight, or access to licensing without physical brick-and-mortar presence requirements, while ensuring appropriate supervision and risk management, can help make banking markets more competitive and resilient. Entry or expansion barriers, by contrast, reduce contestability and may risk fragmenting markets along national lines. Divergent prudential regimes also create opportunities for regulatory arbitrage, as firms may exploit gaps between jurisdictions. In the EU, for example and as underlined in the Draghi Report, completing the Banking Union would help overcome fragmentation, allow genuine cross-border risk-sharing (Draghi, 2024^[98]). At a global level, stronger international co-ordination between prudential and competition authorities may help ensure that cross-border banks and NBFIs operate under consistent standards that protect stability and enable a level playing field.

116. The broader implication is that prudential regulation and competition enforcement may, at times, be complementary and where they conflict, there is an opportunity for balancing. Prudential rules underpin the trust that makes competition meaningful, while competition amplifies the impact of prudential rules by keeping markets efficient, innovative and reducing reliance on a few systemically important firms (Vives, 2016^[4]). Enhanced co-operation enables both sets of objectives to be effectively pursued in tandem: curbing systemic risks, supporting contestability, innovation and fostering efficiency, while improving consumer outcomes. In practice, this likely requires early dialogue, proportionate rule design and institutional and cross-border co-ordination.

4 Conclusion

117. Retail deposit and lending markets are central to economic growth, productivity and financial stability. Prudential regulation underpins the stability and trust on which deposits, credit and investment depend, while competition drives efficiency, innovation and higher-quality financial services. Yet, the interaction between prudential regulation and competition policy can be both complex and dynamic.

118. Prudential safeguards influence the conditions for competition by determining who may enter, operate and exit the market, thereby shaping the structure of core banking markets. Insufficient oversight or an overly narrow prudential perimeter can allow vulnerabilities to accumulate and amplify systemic risk, while poorly calibrated safeguards may unintentionally or unnecessarily discourage competition. Because competition can promote more dynamic and resilient deposit and lending markets, rewarding higher-quality institutions and encouraging innovation, calibrating prudential regulations with awareness of their effects on competition can help sustain both stability and efficiency.

119. Prudential regulations that are proportionate and risk-based can safeguard resilience while maintaining conditions for contestability. Competition policy and enforcement can, in turn, complement prudential goals by preventing the negative effects of excessive concentration and anticompetitive conduct. In practice, the alignment of these objectives may depend on how prudential measures are calibrated, how competition considerations are integrated into their design and how authorities co-operate in monitoring market developments. Key policy considerations in this context include:

- **International co-operation and coherent frameworks can help align objectives.** Consistent approaches to prudential and competition policies can sustain a level playing field and stability as markets evolve and integrate.
- **Co-operation between prudential and competition authorities supports balanced outcomes.** Regular dialogue and joint initiatives, such as sandboxes, market monitoring and forward-looking assessments, can provide opportunities to identify emerging risk, trade-offs, or complementarities.
- **Systematic competition assessments** of new and existing prudential frameworks can help identify and address rules that inadvertently restrict competition while safeguarding prudential goals.
- **Proportionate, risk-based regulation can preserve both resilience and contestability.** Tailoring prudential requirements to risk profiles or complexity may help prevent undue barriers to entry or expansion while ensuring effective prudential oversight.
- **Competitive neutrality can be a helpful guiding principle in balancing objectives.** When crafting prudential rules or measures in the face of trade-offs, the least distortive solutions should be sought in seeking a balance.
- **Credible mechanisms for market exit can contribute to both competition and stability.** Effective resolution tools can enable inefficient institutions to exit the market without contagion or reliance on mergers or state support, while avoiding potential long-term anticompetitive distortions.

120. The interaction between prudential regulation and competition shapes both the resilience and the openness of banking markets. These policies can be most effective when treated as complementary, where possible, or when trade-offs are properly calibrated in light of the other's objectives. Sustained dialogue, proportionate rules and coherent frameworks, domestically and internationally, can help ensure that measures designed to safeguard stability also preserve competition and innovation over time.

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Notes

¹ There is no single global definition of “banking”. In most jurisdictions, however, banks are understood as institutions that take deposits, extend loans, or do both (Ehrentraud et al., 2024^[53]). For this paper, which focuses on retail deposits and lending, the term 'banking sector' (or 'banking markets') encompasses services provided by traditional banks, digital banks (also known as neobanks) and non-bank financial intermediaries (NBFIs). Unless otherwise noted, “banks” refers to both traditional and digital banks (Ehrentraud, Garcia and Quevedo, 2020^[57]).

² Commercial money refers to money created by banks through their lending activities. Unlike central bank money, commercial money is not legal tender but is widely used in transactions and accounts for a significant portion of currency in circulation.

³ Liquidity mismatches occur when the maturity of assets and liabilities do not align, leading to potential solvency problems. Key causes include duration mismatches, where financial institutions invest in long-term assets while relying on short-term funding sources, and behavioural mismatches, such as market panics that cause sudden withdrawals (Carletti and Hartmann, 2002^[5]; OECD, 2011^[2]). Interbank linkages may occur, for example, through interbank lending. This allows banks to share credit risk, but it also enables one bank's crisis to potentially spread across the whole network (Grilli, Tedeschi and Gallegati, 2014^[130]). Informational asymmetries are a defining characteristic of banking markets. For example, when offering credit to borrowers, lending institutions face uncertainty about their creditworthiness. These informational asymmetries may lead to credit rationing and may deviate from the standard results of competitive markets (Dell’Ariccia, 2001^[89]).

⁴ Runs occur when a large number of customers withdraw their deposits simultaneously due to fears that the financial institutions, where these deposits are held, may become insolvent. Contagion refers to the spread of an economic crisis from one institution or market to another, occurring at both domestic and international levels.

⁵ Non-bank financial intermediaries (NBFIs) are also known as non-bank financial companies (NBFCs).

⁶ Systemic risk is the possibility that an event at the company level could trigger severe instability or collapse an entire industry or economy. Certain financial institutions may be deemed systemically important or too big to fail (TBTF) if their failure would cause unacceptable disruptions to the overall financial system. They may be TBTF because of their size or interconnectedness (Labonte, 2018^[131]).

⁷ Actions by depositors can also impose co-ordination and asymmetric information externalities on other depositors. For example, if many depositors withdraw their funds simultaneously, this increases the risk that other depositors lose their money (OECD, 2017^[3]).

⁸ Core micro-prudential instruments may include:

- Supervision and risk management standards aim to identify, measure, monitor and control risk exposures. While tools vary across jurisdictions, they strengthen internal processes such as governance, risk management and strategy. Supervision may also impose ongoing disclosure and transparency obligations, enabling stakeholders to assess institutions' risk profiles. In this way,

supervision complements other micro-prudential instruments and helps address co-ordination and information asymmetry problems.

- Capital requirements or buffers endeavour to ensure that sufficient resources are held to absorb losses and protect depositors and the financial system from insolvency. They are generally risk-based, with higher-risk portfolios requiring higher capital levels. In doing so, they also help limit exposure to mismatches between assets and liabilities.
- Leverage ratios aim to limit excessive borrowing relative to capital. For example, loan guarantees create future obligations that are not yet reflected on the balance sheet. In some jurisdictions, minimum capital is determined not only by risk-weighted assets but also by a leverage ratio, which imposes a floor even when portfolios are considered low risk (Ahrend, Arnold and Murtin, 2009^[1]).
- Liquidity and diversification requirements strive to ensure firms can meet short-term obligations without the need to resort to fire sales or emergency central bank support. They mandate stable funding sources, liquid assets and exposure limits to single counterparties, reducing contagion risk. Such measures are especially important for deposit-takers; credit-only institutions may face lighter or no equivalent requirements (Restoy, 2024^[129]).
- Certification, licensing rules and disclosure requirements aim to ensure new entrants are financially and operationally prepared to conduct business safely. They typically assess capital, business model, governance and risk management. As discussed in Section 2, licensing regimes vary widely across jurisdictions and are a key determinant of market entry conditions in deposit and lending markets (Anginer et al., 2019^[18]; Ehrentraud et al., 2024^[53]). Some jurisdictions permit non-bank financial institutions (NBFIs) to offer limited deposit services, typically excluding demand deposits. Many jurisdictions also permit NBFIs to provide lending services, often under less stringent prudential rules, but with limits to prevent them from holding a significant share of system deposits (BCBS, 2024^[87]).

⁹ Core macro-prudential instruments may include:

- Countercyclical capital buffers require the buildup of capital in booms for release in downturns. They increase system resilience, moderate the financial cycle and mitigate pro-cyclical lending, helping to prevent credit crunches (Coelho and Restoy, 2024^[136]).
- Systemic risk buffers require systemically essential or too-big-to-fail (TBTF) institutions to hold additional capital, reducing the risk of systemic disruption (FCA, 2025^[127]).
- Limits on excessive lending by setting maximum loan sizes against collateral value or borrower income to reduce over-leveraging (Bank of Spain, 2020^[117]).

¹⁰ For example, resolution frameworks exhibit this connection. While they are designed to contain the systemic fallout of a failing institution, they rely on micro-prudential tools that operate at the level of individual institutions, such as imposing loss absorption or recapitalisation requirements.

¹¹ Competition had long been thought to reduce stability by exacerbating risk and reducing banks' incentives to behave prudently. This negative belief has been countered by the argument that competition in the loan market may reduce the risk of banks' portfolios; in addition, the predictions of negative effects of competition on systemic risk have also been challenged (OECD, 2017^[3]).

¹² However, competition may prompt already risky banks to take on even greater risk (Inderst, 2013^[22]). This is why prudential safeguards, as a complement to competition, help safeguard these markets.

¹³ Moral hazard refers to the risk that financial institutions are incentivised to engage in risky behaviour because they do not bear the full consequences of their actions. This is often due to government backing, bailout, or insurance.

¹⁴ For example, the Belgian Competition Authority, in its market study, observed that the four largest banks tend to “ride in peloton,” offering comparable savings products on broadly similar terms, with little variation in interest rates relative to smaller or niche banks (BCA, 2023^[21]).

¹⁵ As highlighted in this Section, switching costs, data asymmetries and consumer inertia are among the most significant structural barriers to entry in retail banking. Together, these frictions weaken consumer mobility, mute price sensitivity and reduce the diversity of providers and competitive pressure. The result is well-documented across jurisdictions: despite wide gaps between introductory and ongoing deposit rates, few consumers switch providers. As a consequence, incumbents face little pressure to raise interest rates for deposits or lower interest rates for loans, while challengers may struggle to attract sufficient customers to compete at scale (ACCC, 2023^[40]; BCA, 2023^[21]; ComCom, 2024^[41]; FCA, 2023^[42]).

The G20/OECD High-Level Principles on Financial and Consumer Protection (2022^[138]) emphasise that consumers should be able to “search, compare, share data and, where appropriate, switch between products and providers easily and at reasonable and disclosed costs, for instance by leveraging interoperable systems.” Across jurisdictions, a range of policy approaches has been used to tackle these barriers and strengthen contestability in deposit and lending markets. They include:

- Consumer education and transparency. Enhanced disclosure of effective interest rates, expiry of bonus rates and fee structures in standardised and easy-to-understand formats can reduce information asymmetries and enable “apples-to-apples” comparisons. Regulatory-led comparison tools can further increase transparency. The UK’s Financial Conduct Authority (FCA) requires clearer savings rate disclosure and publishing of “sunset clauses” on bonus offers, aiming to reduce consumer inertia (FCA, 2023^[42]; 2024^[134]). Similarly, the Belgian Competition Authority recommended reforms to improve comparability and transparency in savings products (BCA, 2023^[21]).
- Simplified switching processes. Switching packs can reduce administrative burdens. These arrangements, often developed through industry self-regulation or competition authority intervention, require banks to handle much of the paperwork to redirect payments and transfer balances (CMA, 2014^[112]). The UK’s Current Account Switch Service (CASS) guarantees account switches within seven working days and redirects payments automatically (FCA, 2015^[124]). While it has reduced technical barriers, behavioural inertia persists, suggesting that switching tools require pairing with transparency and active consumer engagement. Importantly, accounting for behavioural economics insights is also key to tailoring initiatives toward what consumers actually want (FCA, 2013^[143]).
- Data and information portability. Access to consumer financial data can reduce informational switching costs. These can include multiple mechanisms, such as credit information sharing and open banking.

Credit information sharing through public registries or private bureaus is a proven tool for reducing asymmetries and disciplining borrower behaviour (OECD, 2011^[2]). For example, in its Competition Market Study of Tunisia’s Retail Banking Sector, the OECD identified the introduction of market infrastructure, such as credit information bureaus, as potentially important to reducing lending risk by shrinking information asymmetries and reducing the competitive advantages enjoyed by larger banks with larger customer bases (OECD, 2023^[58]). However, while many jurisdictions have national credit information sharing in place, work remains to be done to improve access to credit information across borders (World Bank, 2021^[128]).

Cross-border credit information is becoming increasingly important for competition in deposit and lending markets. As services are provided across borders, national reporting systems may no longer suffice. Without cross-border data sharing, borrowers may face higher costs or exclusion due to the fragmentation of credit information. Conversely, effective cross-border reporting initiatives, such as the European Central Bank’s AnaCredit framework and regional projects in West Africa, demonstrate that greater data availability can reduce information asymmetries and foster competition by enabling new entrants to lend on a sounder

basis (World Bank, 2021^[128]). However, divergent privacy and bank secrecy laws, as well as localisation requirements, are a barrier to cross-border credit information sharing.

Open banking has been adopted in a number of jurisdictions as a pro-competitive regulatory intervention, often spurred by competition authority findings of weak customer mobility in deposit markets and limited contestability in lending. Open banking extends the use of consumer financial data beyond the confines of traditional banks, which historically maintained such information within closed “walled gardens” (OECD, 2025^[45]). By enabling consumers to share their account and transaction data with accredited third parties through secure interfaces, such as APIs, open banking helps reduce information asymmetries that otherwise hinder switching in deposit and lending markets. In doing so, it allows challengers to design competing deposit products or offer credit based on richer, more accurate assessments of borrower profiles.

By broadening data access, such regimes aim to lower barriers to entry, facilitate switching and increase competitive pressure on incumbents to offer better rates and terms, while simultaneously improving prudential outcomes through enhanced transparency. The design of open banking regimes and the accompanying technical standards, differs significantly across jurisdictions. When deciding whether to introduce or refine open banking and related data portability and interoperability frameworks, policymakers benefit from grounding their choices in an assessment of market dynamics, including the degree of competition (OECD, 2025^[45]).

A further barrier identified in many jurisdictions is the bundling of products across banking services, including deposits and lending (BCA, 2023^[21]; ComCom, 2024^[41]). Tying or bundling preferential loan terms to transaction accounts or savings products can increase customer inertia and foreclose single-product entrants. Pro-competitive remedies may include requiring the unbundling of certain products, ensuring transparency around conditional discounts and ensuring the portability of adjacent services when consumers switch accounts. Similarly, measures that promote interoperability across ecosystems, such as enabling portability and interoperability can limit lock-in and support contestability.

Taken together, these barriers, including bundling, switching costs and data asymmetries, limit consumer mobility and blunt competitive pressure. Recent market studies show that addressing these frictions can yield measurable benefits (ACCC, 2023^[40]; BCA, 2023^[21]; ComCom, 2024^[41]; FCA, 2023^[42]). Lower frictions increase demand elasticity, forcing incumbents to raise rates on legacy balances, reduce reliance on reversion pricing and improve service quality. For example, in New Zealand, the Commerce Commission found that lowering barriers to entry and facilitating switching would intensify pressure on incumbents to compete more vigorously, particularly in savings accounts (ComCom, 2024^[41]).

Competition can also enhance prudential regulation's objectives, for example, ensuring that consumers can reallocate deposits away from riskier banks. In markets where switching is a threat, competitive pressures may incentivise better compliance with prudential rules. For example, banks that take excessive risks may be more likely to lose funding and business to safer rivals. Thus, transparency, combined with switching tools, can reduce incentives for banks to take excessive risk.

¹⁶ Conglomerate and ecosystem effects also raise multi-product switching costs. For example, payments provided through digital ecosystems can steer default deposit choices (OECD, 2025^[45]).

¹⁷ The entry of BigTechs brings an entirely different scale and scope to data collection, integrating behavioural, social and transactional data drawn from across their digital ecosystems. Indeed, in some jurisdictions and as markets evolve, banks have sought to match social networking data, including through partnerships with Big Tech companies, with banking data to better understand their clients. This underscores the unparalleled competitive advantage BigTechs may have through their collection and use of data (OECD, 2025^[45]).

¹⁸ BigTech providers particularly count on a significant volume of user adoption as part of their ecosystem offerings. Multiproduct ecosystems refer to groups of complementary or interrelated products and services

that form a bundle for final consumers to use. Engagement across services in an ecosystem may lead to increased switching costs, generating lock-in for customers. BigTech providers' access to user data through their core businesses and related offerings enables the deduction of user behaviour and facilitates the provision of financial services, such as lending. As a result, BigTech providers possess a unique competitive advantage due to their access to user data collected through non-financial activities in their ecosystem. In turn, payments and lending generate more data, thus adding to a platform's value and growth. By integrating mobile payment solutions and lending into their platform ecosystems, BigTech providers can create a lending service that is hard for their potential competitors to replicate. BigTech providers also have unique incentives to provide financial services and, particularly, payment and lending services, as many activities within their ecosystems (e.g., e-commerce) benefit from the ability to realise payments, including those enabled by loans. For example, the growing involvement of BigTech platforms, often through e-commerce or mobile wallets, has shifted lending models toward ecosystem-based provision.

¹⁹ Digitisation has also reconfigured the banks' internal operations and the wider financial services value chain, with growing reliance on outsourced technology services such as cloud computing, cybersecurity and data analytics. This reliance on certain concentrated technology layers can create new forms of operational third-party risk (Restoy, 2023^[107]). For example, a majority of financial institutions rely on a handful of global cloud service providers for critical functions and this dependence is deepening (CSA, 2023^[119]; US Treasury, 2023^[144]; LSEG, 2025^[121]). Given the high concentration in the cloud market, even a single outage could generate systemic effects across the financial sector (ESMA, 2021^[120]; OECD, 2025^[139]). Prudential authorities are increasingly alert to these vulnerabilities (EBA, 2025^[122]). BigTech ecosystems are a particular concern, as disruption in one part of the ecosystem can spill over into others, amplifying contagion across financial and non-financial services. This has raised questions concerning whether traditional prudential tools are sufficient to address concentration and systemic risks when they originate outside the regulatory perimeter (Feyen et al., 2021^[84]; OECD, 2020^[140]).

Policymakers are responding. At the international level, supervisory frameworks are being strengthened, while regional and national initiatives are proliferating. For example, the Basel Committee on Banking Supervision (BCBS) revised its Principles for Sound Management of Operational Risk and Principles for Operational Resilience in 2021 and, in April 2024, added a new Core Principle on operational risk and resilience. In July 2024, the BCBS also launched a consultation on new principles for sound third-party risk management to reinforce banks' operational resilience (Barakova, Ehrentraud and Leposke, 2024^[63]; BCBS, 2024^[118]). In 2023, the Financial Stability Board issued a toolkit to strengthen third-party risk management, while the International Organisation of Securities Commissions and the International Association of Insurance Supervisors developed sector-specific standards (Barakova, Ehrentraud and Leposke, 2024^[63]).

In turn, competition authorities are monitoring how the provision of these technology services may reinforce incumbency across ecosystems or enable exclusionary conduct, including where critical technology providers also compete in payments, lending, or deposits (OECD, 2025^[45]). The OECD's recent work on cloud computing highlights concerns about high egress fees, restrictive discount and credit schemes and interoperability limitations (OECD, 2025^[139]). Such practices can both foreclose entry and expansion by smaller providers and exacerbate operational risks for banks by deepening reliance on a small set of dominant suppliers. Addressing these practices through competition enforcement, therefore, can deliver joint competition and prudential benefits.

In addition to enforcement, pro-competitive regulatory tools can complement prudential objectives. The EU's experience with the Digital Operational Resilience Act (DORA) and the Digital Markets Act (DMA) illustrates how prudential and competition policies can address different facets of technology reliance and intermediation in complementary ways. DORA addresses the prudential risks of systemic dependence on a few technology providers by creating a prudential oversight regime for these third-party providers. DORA

effective from 2025, establishes a harmonised framework for managing information and communication technology (ICT) risk. DORA explicitly extends oversight to critical third-party providers, including cloud operators, giving European Supervisory Authorities direct supervisory powers to address systemic dependencies (EBA, 2023_[123]). In turn, the DMA targets some of the same firms, designated as digital gatekeepers, with the aim of making markets contestable. In sum, the benefits of close co-operation between prudential and competition authorities may be heightened by digitisation and rising areas of joint concern and they can benefit from futureproofing for risks, as discussed in Section 3.3.

²⁰ For example, the OECD in its Competition Market Study of Tunisia's Retail Banking Sector found that the licensing process for payment service providers creates unnecessary barriers to entry, by introducing capital requirements that are between 12 and 76 times higher than capital requirements for similar service providers in the EU (OECD, 2023_[58]).

²¹ Modern international prudential standards, applicable to financial institutions, have evolved over more than three decades, driven by successive crises that exposed weaknesses in prudential rules. The key standards include:

Basel I (1988) was the first internationally agreed framework, focusing primarily on prescribing minimum capital requirements for financial institutions to reduce credit risk. Under this framework, assets are classified according to their risk level and financial institutions are required to maintain at least 8% of their determined risk profile on hand.

Basel II (2004) expanded the capital framework through its “three pillars” approach, including: (i) minimum capital requirements with more risk-sensitive methodologies, (ii) supervisory review and (iii) market discipline measures enabled through disclosure (BIS, 2005_[132]).

The 2007-2009 global financial crisis revealed shortcomings in capital quality, liquidity management and the absence of systemic risk tools. For example, while Basel II intended to align capital more closely with risk, its reliance on regulated institutions' internal models later drew criticism for underestimating some exposures and contributing to undercapitalisation in the lead-up to the global financial crisis (White, 2014_[11]).

In response, **Basel III (2010)** enhanced existing risk-based capital rules and imposed new requirements on leverage, liquidity and significant exposures. Other important measures include more intensive supervision, resolution regimes and resolvability requirements for systemically important firms. In addition, enhanced accounting standards have been adopted to prompt banks to recognise credit losses earlier in the credit cycle. The reforms also introduce a macroprudential overlay aimed at limiting systemic risk, including countercyclical capital buffers and other macroprudential measures.

Established by the Basel Committee on Banking Supervision (BCBS), the fundamental objective of the Basel standards is to ensure consistent prudential requirements across jurisdictions, thereby maintaining a global level playing field and fostering global financial stability. As of 2025, more than 100 jurisdictions have committed to implementing Basel III standards through national legislation (Hohl et al., 2018_[8]). However, the degree and pace of adoption vary across jurisdictions (Coelho, Restoy and Zamil, 2020_[133]). Currently, many jurisdictions are implementing the final elements of Basel III. Differences in adoption have been identified as a source of market fragmentation. Such fragmentation not only undermines global prudential consistency but may also weaken competition by discouraging cross-border entry.

²² Different types of deposits include:

- **Demand deposits.** Funds are held “at call,” which means that customers can access funds held within these accounts at any time, instantly, on demand. Typically, deposit accounts are those where customers receive income and other funds and from which they conduct everyday financial activities such as paying bills, groceries, entertainment, etc. For this reason, transaction accounts are also known as current accounts. They are also typically linked to debit cards. These accounts often have

high cash flow rates. That is, often receiving funds such as income and depleting funds until the next pay cycle (ABA, 2023^[113]; Federal Reserve, 2025^[114]).²²

- **Savings accounts.** Funds are held “at call,” and customers can typically access funds on demand, nearly-instantly. However, these accounts usually cannot be linked to a debit card, which means they need to be transferred from the savings account to be used for purchases. Direct debits are typically not possible from these accounts either. The benefit of these products is that they tend to accrue higher interest than transaction accounts. Thus, customers usually use these accounts to build up a pool of savings (Siroto, 2025^[99]; Federal Reserve, 2025^[114]).
- **Term (or time) deposits.** Funds are typically held within the deposit account for an agreed period. This is a savings account that allows customers to receive higher interest rates in return for the unavailability of the money for a specified period of time. If needed, customers can recover the funds placed in the term account before the expiration date, but this typically entails penalties, as outlined in the initial contract. An example of a term deposit is a certificate of deposit (Federal Reserve, 2025^[114]; Service Public, 2025^[115]).

Retail deposit products typically have different interest rate structures. The rate a consumer receives may depend on their available balance and its size, as well as other personal characteristics, including how they use the product. Interest rates namely apply to savings accounts and term deposits, as transaction accounts tend to have negligible or no interest rates available (ACCC, 2023^[40]). Examples include:

- **Base interest rates.** These rates are generally available to all holders of deposit products; they represent the minimum or base interest rate available.
- **Introductory interest rates.** These rates are offered when a customer opens an account and are typically higher than the base interest rate with a short initial duration.
- **Bonus interest rates.** These are conditional interest rates that are added on top of the base interest rate if a consumer meets certain conditions, such as growing the account balance to a certain amount, making a certain number of transactions, or limiting withdrawals.
- **Headline interest rates.** These represent the total interest rate for a deposit product, including the base interest rate and any introductory or bonus interest rates.
- **Fixed-term interest rate.** Term deposits typically have fixed interest rates which do not change during the duration of the fixed term.
- **Tiered interest rate.** These rates may apply and vary depending on the deposit balance.

²³ Diverging licensing regimes may include:

- **Full banking or omnibus licenses** allow for both deposit-taking and lending, amongst other services. This type of license carries the highest prudential obligations, including compliance with capital, liquidity, leverage and governance standards. It also frequently requires participation in deposit guarantee schemes.
- **Monoline licenses** permit a single service to be conducted by a licensed entity (Ehrentraud et al., 2024^[53]).
- **Deposit-taking licenses** are typically required across jurisdictions for institutions that accept retail deposits from the public. They often impose entry requirements, such as minimum initial capital requirements or leverage standards, reflecting the systemic importance of deposits. Across most jurisdictions, monoline licenses are not available for deposits. Typically, if these are available, it is for certain types of limited deposits, such as term (or time) deposits, but not demand deposits.
- **Credit-only licenses** are available in some jurisdictions for institutions that engage solely in lending without deposit-taking. Prudential obligations are typically lighter. These may include lower or no capital

thresholds, minimal liquidity requirements, or no leverage ratios. However, these institutions may face higher funding costs without access to deposits, which would hinder their ability to provide loans.

²⁴ For example, in Australia, Brazil, the People's Republic of China (China), Colombia, Hong Kong (China), India, Singapore, South Africa, the UK and the US, entities that take demand deposits are required to hold a banking license (Ehrentraud et al., 2024^[53]; Federal Reserve, 2025^[114]; PRA, 2025^[116]). A notable exception is Argentina, where the Central Bank currently allows NBFIs to accept both demand and term deposits (Ehrentraud et al., 2024^[53]; Central Bank of Argentina, 2024^[100]; Ministry of Justice of Argentina, 1977^[101]). In Argentina, pursuant to Article 24 of Law No. 21.526, finance companies are permitted to accept time deposits, while demand deposits are not mentioned as a permissible activity. However, Article 20 allows the Central Bank of Argentina to expand the scope of activities that finance companies may undertake. Based on this power, the central bank currently allows finance companies to accept time and demand deposits (Ehrentraud et al., 2024^[53]). Argentina's economic policy is unique: the Central Bank is reengineering domestic regulation to restore macroeconomic stability and overcome shallow financial markets, with the aim of crowding in private-sector credit while preserving stability (Central Bank of Argentina, 2025^[105]).

²⁵ In the EU, generally, any person other than a bank is prohibited from taking deposits or other repayable funds from consumers. However, national exemptions apply.

²⁶ For example, deposit-taking NBFIs in India are required to obtain an investment-grade rating or higher on an annual basis. If a deposit-taking NBFI loses its investment grade rating, it cannot renew existing or solicit new term deposits (Reserve Bank of India, 2025^[110]; Ehrentraud et al., 2024^[53]). These conditions can themselves act as bottlenecks to competition and thus may also be crafted with balance in mind. For example, while requiring external ratings helps investors gauge risk, reliance on credit ratings also raises concerns and can introduce competition distortions (Camanho, 2020^[102]; Bongaerts, 2014^[103]; Crenshaw, 2023^[104]; Bush, 2022^[137]).

²⁷ For example, in India and Hong Kong (China), NBFI deposits are not covered by deposit guarantee schemes, although these companies are allowed to offer term deposits. Other jurisdictions, such as Argentina, Brazil, Colombia, New Zealand and Singapore, cover NBFI deposit holders under deposit guarantee schemes.

²⁸ A deposit guarantee scheme or deposit insurance is a system designed to protect depositors and provide insurance for their funds. It is a safety net that ensures, up to a certain level, of deposits will always be repaid, even if the bank holding them fails or goes insolvent (EBA, 2024^[64]). Participating institutions usually fund the scheme through contributions.

²⁹ Prudential regulations for retail lending vary widely. Some jurisdictions extend all elements of the banking prudential framework to NBFIs. Others focus mainly on conduct and consumer protection. In some countries, multiple licences are required to carry out all lending activities; in others, a single authorisation is sufficient. In some cases, certain credit products may be unregulated or only subject to registration requirements (Ehrentraud et al., 2024^[53]). For example:

- **Omnibus credit licenses.** In Argentina, Australia, Japan, Brazil, Mexico, Indonesia, Hong Kong (China) and Singapore, NBFI lenders who hold the relevant omnibus credit license are enabled to offer all credit types (Ehrentraud et al., 2024^[53]).
- **Monoline credit licenses.** In Egypt, Sweden and the US, monoline licenses are available depending on the type of credit an NBFI is keen to offer (Ehrentraud et al., 2024^[53]).²⁹
- **Registration.** In Argentina, Colombia and South Africa, NBFIs do not require a license, but need to register with the relevant authority to operate (Ehrentraud et al., 2024^[53]).

- **No license or registration.** Many jurisdictions do not require either a license or registration for NBFIs lenders. Moreover, across jurisdictions, NBFIs often operate without licenses: instead, credit is provided in partnership with banks, as discussed in Section 2.1.

³⁰ Different types of loans include:

- **Secured loans.** A secured loan is backed by collateral, which can be the asset that the loan is financing (e.g., a house or a car) or another form of pledged property. The purpose of collateral is that if a borrower defaults on a loan, the lender can take possession of the collateral to recoup their losses. Secured loans are typically for a term, repaid in instalments until the loan is paid in full at the end of its term (van Hoenselaar et al., 2021^[141]).
- **Unsecured loans.** An unsecured loan does not require any collateral. Lenders generally rely instead on a borrower's creditworthiness and income to assess repayment risks of providing a loan. Common examples include personal loans, personal lines of credit, student loans and credit cards. Unsecured loans can be revolving or for a term (FSB, 2011^[125]).
- **Revolving loans.** These loans are open-ended credit lines; they have credit limits that can be spent, repaid and then spent again. A credit card or an overdraft on a deposit account is an example of a revolving unsecured loan.
- **Term loans.** These loans are repaid in instalments until the balance is paid in full at the end of the term.

Interest rates for loans also vary, including by loan and risk type. They represent the amount a lender charges a borrower and this is typically a percentage of the principal amount loaned. The perceived risk of a borrower defaulting on a loan is generally part of the calculation of the interest rate. If a borrower is perceived as low risk, this usually means a lower interest rate. If the loan is considered high risk, then the borrower is charged a higher rate.

Secured loans typically offer a lower interest rate, given that collateral is provided, lessening the perceived risk. In contrast, unsecured loans usually have higher interest rates, as the lack of collateral augments the perceived risk. Moreover, interest rates may be fixed or variable. Fixed interest rates remain constant throughout the term of a loan, while variable interest rates may vary based on market conditions. For example, credit cards often have variable interest rates. Some jurisdictions, however, may impose minimum or maximum rates, or other limits to interest rates, according to the relevant type of product (FasterCapital, 2025^[106]).

From a prudential perspective, secured loans generally carry lower risks due to collateral. However, they do expose lenders to collateral valuation risks and longer maturities (e.g. mortgages). Unsecured loans tend to have higher credit and operational risks but shorter maturities and thus may be subject to lighter prudential treatment, including for non-banks. In other words, these distinctions may justify different licensing and capital regimes across jurisdictions.

³¹ Wholesale funding refers to raising funds from institutional investors and financial markets. Securitisation involves pooling assets, such as mortgages, credit card receivables, or other loans and issuing interest-bearing securities backed by that pool (ACCC, 2023^[40]).

³² Some NBFIs activities may resemble shadow banking insofar as they replicate credit intermediation outside the full prudential perimeter. These risks are typically associated with wholesale markets, securitisation and money market funds. As such activities differ from the retail deposits and lending focus of this paper, they are not explored further in this paper.

³³ Since 2007, banks in many jurisdictions have shifted their funding mix away from short-term wholesale debt and securitisation toward deposits. This reflects a post-crisis reassessment of liquidity risks, as banks recognised the vulnerability of unstable short-term markets and the introduction of prudential reforms, such as the liquidity coverage ratios (LCR) under Basel III, that incentivise more stable, deposit-based funding structures (ACCC, 2023^[40]; BCBS, 2024^[87]).

³⁴ In many jurisdictions, large banks often enjoy lower funding costs in wholesale debt markets than smaller banks, for example. This may reflect credit rating agencies' assessments of their broader diversification, scale and the perceived likelihood of government support, which can translate into higher ratings. As a result, larger banks may secure wholesale funding on better terms and, in some cases, can also access international markets more easily due to stronger ratings, name recognition and the ability to issue larger, more liquid instruments (ACCC, 2023_[40]). In addition, another advantage present for incumbent banks, when certain regulatory conditions are met, is that securitisation may lower the amount of capital a bank must hold against those exposures, which can, in turn, free up balance sheet capacity to support additional lending or growth (ACCC, 2023_[40]; BoE, 2023_[111]).

³⁵ In some jurisdictions, for example, regulators impose minimum paid-up capital thresholds, leverage or liquidity limits in lieu of capital requirements to non-deposit-taking NBFIs of a certain size. As discussed further in Section 3, India's scale-based framework is an example of a system that imposes such a prudential requirement (Reserve Bank of India, 2025_[110]). Other jurisdictions focus on conduct supervision without specific capital rules, as deemed necessary, depending on the lending product (Ehrentraud et al., 2024_[53]).

³⁶ In 2022, NBFIs, including BigTechs and FinTechs, held a 22.5% share of all credit assets, compared with banks' 65.5% (Ehrentraud et al., 2024_[53]). BigTechs overtook FinTechs in credit provision in 2023 (Cornelli et al., 2023_[142]).

³⁷ Peer-to-peer lending, crowdfunding and multiple other sources of credit, fueled by digitisation, have also risen in recent years. However, these types of lending are kept out of the scope of this paper (Ehrentraud et al., 2024_[53]).

³⁸ BNPL also raises consumer protection risks. For more information, see the Council report on the implementation of the OECD Council Recommendation on consumer protection in the field of consumer credit: note by Secretary General (OECD, 2025_[135]).

³⁹ For example, in the US and EU Member States, the number of banks declined both before and after the global financial crisis (Vives, 2016_[4]). Notably, in the EU, concentration has increased significantly in local markets. For the avoidance of doubt, this assessment does not take a position concerning cross-border mergers. Where the merging firms do not compete in the same geographic markets, such combinations may constitute entry or increased competitive pressure into new geographies and may be pro-competitive or competition-neutral where local overlaps are non-existent or limited, and no other potential for the substantial lessening of competition is found. That said, facilitating foreign bank or foreign NBFIs entry into markets through well-calibrated regulation, rather than limiting entry paths for foreign banks to acquisitions, may be a more pro-competitive alternative (Anginer et al., 2019_[18]).

⁴⁰ A further challenge is the limited visibility regulators have into these partnerships, making it difficult to assess and monitor their risk (BCBS, 2025_[83]). Recognising this, regulators in multiple jurisdictions have begun systematic reviews, including the European Supervisory Authorities (ESAs) 2024 review of BigTechs in finance and the US Federal Banking Agencies' consultation on bank-fintech arrangements (Barakova, Ehrentraud and Leposke, 2024_[63]). The ESAs highlighted the difficulty of identifying appropriate supervisory counterparts across borders, pointing to the need for stronger co-operation between prudential and competition authorities (ESAs, 2023_[126]).

⁴¹ As highlighted by the OECD in its Competitive Neutrality Toolkit, in some instances, it may be good practice to treat incumbents and smaller competitors or potential competitors differently to promote contestability. By imposing asymmetric obligations on specific firms, the playing field may be levelled by promoting entry and preventing smaller competitors from being excluded from the market (OECD, 2024_[81]). As underscored by the OECD's Recommendation on Competitive Neutrality, a key element to ensuring regulations remain pro-competitive includes continuous monitoring, including evaluating regulations through competition assessments and the ability to redesign, restructure, or withdraw a policy as needed.

⁴² The 2019 OECD Recommendation on Competition Assessment and Toolkit can help governments improve their laws and regulations and promote more competition in their economies, leading to lower prices, greater choice and higher quality of goods and services. The Toolkit helps identify laws and regulations that can restrict competition and supports governments in looking for alternative ways to achieve policy objectives (OECD, 2019^[91]).

⁴³ In Australia, the ACCC found that incumbent banks were slower and more selective in raising deposit rates than smaller rivals, with pass-through particularly limited for customers in basic, high-volume products (ACCC, 2023^[40]). The Belgian Competition Authority similarly concluded that incumbent banks' dominance contributed to significantly weaker savings rate pass-through than in neighbouring countries, with complex dual-rate structures further reducing comparability and competitive pressure (BCA, 2023^[21]). New Zealand's Commerce Commission highlighted a "stable oligopoly" of four major banks and identified a lack of competition as a factor reducing incentives to improve deposit offerings (ComCom, 2024^[41]). The UK FCA has likewise pointed to structural concentration and low switching rates as drivers of limited pass-through in retail banking markets (FCA, 2023^[42]).

⁴⁴ This paper does not take a position for or against these measures. However, it is important to note that they do not address the underlying structural drivers of the pass-through problem itself. Since the financial intermediation role of banks is to direct savings into profitable investment projects, the margin between the interest rate banks pay for their funds (including deposits and other forms of borrowing) and the interest rate charged for loans can be interpreted as a measure of competition and efficiency (Demirgüç-Kunt and Huizinga, 1999^[109]). Thus, the most suitable solution to address pass-through issues may be to increase competition. Lower interest margins can result from lower rents or a more immediate passing on of cost reductions to customers, which indicates more intense competition among banks. From a prudential perspective, narrower margins achieved through competitive pressure may enhance efficiency and monetary policy transmission, while persistently wide margins may signal weak competition, excessive rents and potential prudential concerns.

⁴⁵ Further competition-enabling recommendations are included in the market studies. For example, the Belgian authority makes multiple recommendations to stimulate competition in the retail banking market, without jeopardising its stability. These include considering product separation and a principled ban on tied sales and other bundled offers, subject to certain exceptions that benefit customers' interests, with the aim of enhancing contestability and reducing customer immobility (BCA, 2023^[21]). Similarly, the ACCC's inquiry into retail deposits noted that strategic product design by large incumbents, including the setting of discretionary conditions on high-interest products, could be scrutinised where such design features restrict effective competition (ACCC, 2023^[40]). By addressing such practices, competition enforcement can help ensure that competitive pressure drives improvements in the rates offered to depositors, thereby supporting the transmission of monetary policy.

⁴⁶ By contrast, windfall taxes respond to the distributional consequences of weak pass-through without necessarily altering the incentives or conduct of banks. Strengthening competition enforcement and adopting competition-enabling policy tools, such as open banking, centralised comparison platforms and restrictions on exclusionary product design, may thus contribute to alleviating concerns about monetary policy effectiveness. In this way, competition policy and enforcement can complement prudential regulation and broader macroeconomic objectives, ensuring that interest rate changes are more effectively transmitted across the financial system and to consumers.

⁴⁷ Simpler rules can improve transparency and supervisory effectiveness, while lowering compliance costs for smaller and less complex institutions, thereby supporting entry and a level playing field (Cannata and Serafini, 2025^[108]).