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Balancing Prudential Regulation and Competition Considerations in Banking – Note by Spain

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1. Introduction

1. The relationship between competition and financial stability (and, by extension, prudential regulation) has been the subject of extensive theoretical and empirical analysis. However, the evidence remains inconclusive regarding the direction of their interplay, highlighting the need for a case-by-case approach.
2. Market failures are present in the financial sector. Therefore, markets *per se* do not lead to efficient outcomes, generating the rationale for public intervention. But that intervention must be optimally designed to improve efficiency *vis-à-vis* the market. Otherwise it may not necessarily improve market outcomes.
3. The CNMC has developed the policy insights contained in this contribution through its competition advocacy role. This paper summarises several of its key initiatives in this regard.
4. Following this first introductory section, Section 2 discusses the [market study on the impact on competition of new technologies in the financial sector](#), i.e. the Fintech phenomenon. Section 3 refers to a [report on the remuneration on deposits](#) and a [report on the potential reform of the financial sandbox regime](#). Section 4 outlines the main conclusions.

2. Market study on Fintech

5. In 2018, the CNMC conducted a [market study on the impact on competition of new technologies in the financial sector](#), commonly referred to as the Fintech phenomenon. The CNMC was very active in trying to spread out the content and recommendations of the report. Apart from the [report itself](#) and the [press release](#), the CNMC actively disseminated the findings and recommendations of the study through various channels, including a blog post¹, a explanatory video² and two workshops³). The CNMC has also explained in detail this market study in previous contributions to the OECD⁴.
6. The report aimed to add value in several aspects.

¹ <https://blog.cnmc.es/2018/11/13/que-es-fintech-las-claves-de-la-nueva-tendencia-del-mercado-financiero/>

² <https://www.cnmc.es/node/379007>

³ <https://www.cnmc.es/jornada-fintech>

<https://www.youtube.com/watch?v=XDXcLtGqQAU>

<https://www.cnmc.es/jornadas/fintech-oportunidades-y-retos-para-el-consumidor-y-la-promocion-de-la-competencia>

<https://www.youtube.com/watch?v=GUxExLSZCZM>

⁴ <https://www.oecd.org/en/events/2024/10/latin-american-and-caribbean-competition-forum-2024.html#fintech-open-banking>

https://www.cnmc.es/sites/default/files/promocion/consultas/2019-06/DAF-COMP-WD%282019%2931.en_.pdf

- First, by carrying out an **analysis of the financial sector from a competition advocacy approach**. Financial sector exhibits all the types of market failures, imperfect information (risk and uncertainty) being perhaps the most paradigmatic. But there are also barriers to entry due to scale⁵/scope/network economies, externalities (imprudent conduct of some agents may affect others and the system in general) and public good characteristics (like the case of financial stability). Some of these features (scale⁶/scope/network economies) lead to market concentration.

Yet, at the same time the financial sector is one of the most heavily regulated industries, and regulation itself may introduce additional barriers to entry, potentially exacerbating concentration.

The study⁷ explored this dynamic, particularly the role of prudential regulation, which—while addressing market failures—can also limit competition by raising entry barriers.

- Second, by **defining and mapping Fintech initiatives**. According to the market study, Fintech consists of the disruptive application of new information and telecommunications technologies (ICT) to the financial system. Therefore, Fintech innovations are not mere “incremental” improvements of traditional business models (e.g. incumbents introducing mobile and online banking). Fintech innovations are substantial and disruptive, introducing digital tools in the production function (e.g. big data and artificial intelligence), boosting productivity, reducing infrastructure costs, slashing back-office expenses by automating or streamlining tasks, increasing convenience for customers, etc.

Against this backdrop, the study describes the sectoral dimensions of the Fintech phenomenon: neo-banks, distributed ledger technologies (DLTs such as blockchain), innovative payment systems, automated asset management and advice (such as robo-advisers), crowdfunding and Insurtech. For each sectoral dimension of Fintech the study assesses advantages and opportunities and risks and challenges for competition. All that in order to derive implication from the standpoint of competition advocacy and good regulation principles.

- Third, by providing specific **conclusions and policy recommendations**. The study concluded that Fintech innovations have a notable potential to improve competition and efficiency, especially by addressing some of the market failures which were inherent to financial intermediation. Therefore, the rationale for some forms of regulation and the specific design of the regulation may be reconsidered, like in the case of prudential regulation.

The study specifically advocated for changing the scope of regulation: moving from the regulation of entities to the regulation of activities, since the market failures are linked to the latter (and not the former). As a corollary to this, reserves of activity to specific entities would not be justified.

The study also suggested considering the introduction of innovations in regulatory compliance (Regtech) to lower the burdens associated to regulation and supervision.

⁵ Both static (due to fixed costs and increasing returns) and dynamic (learning-by-doing).

⁶ Both static (due to fixed costs and increasing returns) and dynamic (learning-by-doing).

⁷ https://www.cnmc.es/sites/default/files/2218346_1.pdf See paragraphs 2.19 to 2.24.

7. Finally, the study specifically recommended the development of a regulatory sandbox to ensure that new innovative business models could develop without the initial burden of a heavy entry regulation. **This recommendation of adopting a regulatory sandbox was later followed, since the [Parliament approved a law](#) introducing it.**

8. Though published several years ago, the study's findings remain relevant and continue to inform the CNMC's monitoring and advocacy work in the financial sector, as evidenced by the two recent reports discussed below.

3. Current initiatives from the standpoint of competition advocacy

9. Since publishing its Fintech study, the CNMC has continued to monitor the intersection of competition and regulation in financial services. Two recent initiatives—both commissioned by the Ministry of the Economy—are particularly noteworthy.

3.1. Report on factors affecting deposit remuneration

10. The [report on the factors affecting remuneration on deposits](#) was released in January 2025. It showed that deposit remuneration in Spain was significantly lower than in the Euro Area, both for households (0.48% in Spain vs 1.17% in the Euro Area) and firms (1.22% in Spain and 1.60% in the Euro Area).

11. The degree of concentration varies among the different Spanish regions, but it is especially high in provinces where population is concentrated in small towns. The qualitative and the econometric analysis included in the report suggested that market concentration, on their own, is not sufficient to assess the intensity of competition in the deposit market. Other factors of relevance could be switching costs (lock-in effects due to loyalty discounts, lack of comparability and practical difficulties in account portability), limited competitive pressure from alternatives (other investment products or digital-only banks) and low financial literacy among consumers.

12. The report issued recommendations to:

- **Improve consumer access to a wider array of products**, including public-private partnerships in financially excluded areas (where alternative to traditional banks are not developed).
- **Mitigate customers' information problems through training initiatives and greater transparency**. In particular, strengthen and better coordinate existing financial education and digital-skills initiatives. Improve transparency in deposit offers, especially by setting standards for comparison websites and expanding the scope of the public comparison tool. Provide regular information from institutions to their customers.
- **Reduce switching costs and enhance portability between institutions**, including regarding contracting deposits with foreign institutions.

3.2. Report on the potential reform of the financial sandbox regime.

13. The government sent to the CNMC, in its advisory role, a draft law considering potential reforms of the sandbox regime, which had been introduced in 2020, after the CNMC had issued its market study on Fintech.

14. The CNMC issued its [report](#) in June 2025. In general, the CNMC endorsed the main aspects of the reform, which could contribute to the deepening of the European internal

market for financial services, while expanding the access of new modes of service provision to the financial sandbox. **Many of its measures are in line with the recommendations made by the CNMC in its [Fintech market study](#).** Particularly noteworthy are the provision for new payment solutions and digitalization and the update of the financial sandbox.

15. Nonetheless, the CNMC included several recommendations in its report:
- **Ensuring continuous access to the sandbox**, avoiding arbitrary deadlines that could lead to unequal treatment.
 - **Guaranteeing that participation in the sandbox is without prejudice to compliance with competition policy.**
 - **Avoid imposing advertising restrictions** (e.g., on crypto-assets) unless clearly justified by the principles of necessity and proportionality.
16. The reform has not yet been finalized, and it remains unclear to what extent these recommendations will be adopted in the final legislation.

4. Conclusions

17. The CNMC analyses on the financial sector shows that prudential regulation can be balanced with competition considerations in banking. It is therefore concluded that financial stability (together with other legitimate public goals) can be attained at the minimum costs for competition and efficiency.

18. Recent developments in the financial sector (such as Fintech) increase the rationale for revisiting prudential regulation, even if the causal relationship between competition and stability in the financial sector has to be assessed with a case-by-case approach.