Why does financial regime governance have these limitations?

chapter 10

1. Why is the pace of financial innovation slow?

The design of a reforms process aimed at improving financial regime governance needs to flow from a diagnosis of the sources of difficulties. There are a number of obvious operational reasons as well as proximate reasons and deeper sources of dysfunction.

1.1. Regulators are preoccupied with averting scams

In an ideal world, regulators evaluating their impact on financial system development need to weigh in a balanced fashion three important factors: (a) encouraging progressive improvement in the capability of the domestic financial system; (b) improvements in its global competitiveness; and (c) the risk of financial regime reputation loss in the event of firm/market failure or default. However, the incentive structure faced by regulators in India attaches low priority to improving the quality of domestic resource allocation by financial markets, or on achieving greater international competitiveness. Indian regulation appears disproportionately focused on averting financial scams. This generates a regulatory bias of blocking innovation in order to be safe, and an industry bias of avoiding untested ideas since they expose firms to indirect risk when the next failure occurs.

A more nuanced but realistic regulatory perspective might be to recognise that accidents will happen even with the best regulation. But they will be fewer and less fatal. The only way to avoid accidents altogether is to choke traffic with too many roadblocks, or stop it from flowing altogether. Air-crashes occur; but that does not imply airlines should be regulated out of flying or, because road crashes occur, that no traffic should be allowed to flow. In India financial regulation has put so many roadblocks in place that financial innovation can only occur at a snail's pace. Worse, the road to financial innovation in the 21st century cannot be travelled at any speed by regulation that results in India's financial firms remaining the equivalents of antediluvian Ambassadors and Fiats in India's financial services industry when the rest of the world is using BMWs and Ferraris. Every year, the gap between Mumbai and London is growing, not narrowing.

A more appropriate regulatory view might be to accept that even the best-regulated financial system will have some small problems (of less than say Rs. 500 crores or Rs. 5 billion). That is one basis point compared to total financial assets of over Rs. 50 lakh crores (Rs. 50 trillion). The *efficient* safety level is not 100%. Each percentage of point of safety beyond 97% has a disproportionately higher cost; one that increases in logarithmic rather than linear fashion – and one that is not worth expending.

In that context it should be noted that the evidence accumulated over the last decade in the UK (when compared to the US) suggests that ***principles-based regulation*** might be more effective than rules-based regulation, in averting damaging financial malfeasance. **That is because it requires financial firms to conform not just with the letter of the law (rules/regulations) but with its spirit as well.** It co-opts the financial firm into becoming an integral player, along with the regulator, in a cascading and co-operative (rather than adversarial) process of self-regulation at the level of the individual, firm and market. Principles-based regulation avoids the risk of turning financial firms (as well as their lawyers, accountants and tax advisors) into guerilla game-players that ceaselessly focus on beating or side-stepping the rules in order to gain a competitive edge in the financial marketplace.

A rational cost-benefit analysis in the form of regular 'regulatory impact assessments or RIAs' (standard practice in most OECD countries) therefore needs to be undertaken to compare the cost of inefficient resource allocation (*e.g.*, through financial preemption) against the cost of tolerating the occasional small scandal by loosening regulation to permit more financial flexibility and innovation. Such an analysis might suggest that: achieving allocation efficiency through better functioning of the financial system with an investment ratio of 30% of GDP (*i.e.*, Rs. 10 trillion) per year, and the avoidance of financial preemption, might be important enough to pay for a scandal costing around 0.1% of GDP (roughly Rs. 33 billion) once every few years.

1.2. A *de facto* shift towards over-prescriptive regulation in India

Given its legal heritage, India started out with a more open basis of law based not on exclusive reference to a codified constitution, but on equal respect for the evolution of precedent based on trial-and-error. But over time it has moved relentlessly toward a style of regulation under which every minute detail is either written into the basic legislation or into detailed subordinated rules and regulations. Under such a system if something is not specified, it is proscribed; or conversely, if something is proscribed then non-proscribed activities remain contentious as to whether they are permissible or not.

For example, a SEBI Committee on Gold ETFs did the kind of preparatory groundwork that a financial firm, and not a regulator, should do – *i.e.*, it designed an alternative product structure. In the prevailing financial governance regime, every detail of financial product and market mechanism is written down in meticulous detail either in the law or in subordinated legislation. The consequence of this approach is that every financial innovation requires interminable changes to be made to either governing laws, subordinated regulations or both. This raises the cost of innovation considerably. It deters financial firms from innovating because the returns from investment in innovation are rendered uncertain.

By contrast in the UK the approach to regulation permits financial innovations to be tried and tested almost instantaneously by financial firms in markets with large sophisticated customers at their own risk and with full customer awareness. If the innovation works, the regulators step in to see how the risk involved (to customers, firms and markets) can be diminished and managed better until the product becomes accepted as standard. This more innovation-friendly approach perhaps explains why London is so successful as an IFC while financial frauds of Enron, Worldcom, Tyco and Arthur Andersen dimensions continue to occur in the US despite the best rules-based regulation in the world.

1.3. Regulatory architecture

A major source of delay is fragmentation among regulators and uncertainty about which one will regulate new instruments and markets. Modest innovations like the Gold ETF, interest rate futures or currency futures – which would not be called innovations outside the country given their extreme degree of obviousness – run afoul of inconsistencies and turf battles across the multiple regulatory agencies. The problem is particularly acute with organised financial market trading, regulatory responsibilities for which are spread between three regulators: commodity derivatives are regulated by the Forward Markets Commission (FMC); equity spot and derivatives and corporate bonds are regulated by SEBI; government bonds and currency trading are regulated by RBI.

1.4. Lack of competition

The: (a) lack of sufficient competition in the financial services industry: (b) pervasiveness of public ownership; and (c) over-compartmentalisation of sub-sectors; result in easy profits being made through sub-optimal performance by existing players. Clearly the situation has improved since 1992. But much remains to be done to introduce greater competition in Indian finance; especially in banking services.

That competition needs to be across larger, more capable players rather than among a plethora of small weak, under-capitalised players that cannot capture economies of scale or make the kinds of investments in people, training, technology and research into product development that supports innovation. The Indian financial sector needs a wave of consolidation – through acquisitions and mergers, among private and publicly owned institutions – for its financial firms to be strong enough to compete as aggressively with each other, and with foreign firms, in Indian and global markets as they should. A license to operate in a certain area of Indian finance is, all too often, a safe sinecure with stable profits and a near-zero probability of death. There is therefore little incentive to innovate to remain competitive. This is not unlike firms in the real economy before 1992.

For a shift into a high-innovation regime, both carrot and stick are required. The stick would be the introduction of competition: entry barriers in domestic finance and protectionism need to be removed. The carrot would be the significantly reduced cost of innovation that would result from a different regulatory attitude and approach. In addition, a shift from a domestic-focused financial sector to an IFS-focused financial sector would induce the associated carrot of enormously larger market size.

2. Proximate underlying reasons that are not as transparent

To some extent, these constraints to innovation are a hangover of the system of controls that pervaded the Indian economy in preceding decades. Once policy makers become aware of the deleterious consequences of these aspects for India's ability to build export-oriented IFS, progress should be relatively easy to make. However, far-reaching progress – which is of essence in achieving the goal of making Mumbai an IFC – will not be made until the 'proximate reasons' and 'deeper sources' of these problems are addressed. A strategic understanding of the reform effort that is required for making Mumbai an IFC requires an understanding of these proximate reasons and deeper sources.

2.1. Financial preemption

In a mature market economy, finance must interact productively with the decision-making of private economic agents and shape the resource allocation emerging out of these decisions as efficiently as possible. But Indian finance has a history of financial preemption. Formerly, the task of finance was seen as mobilising resources for the implementation of socialism at two levels: first, to fund fiscal deficits on below-market terms and second, to direct the supply of resources into socially important areas under the guidance of planners rather than the rules of the market.

Most policy-making in finance in past decades, has been shaped by financial repression: *i.e.*, forcing finance to allocate resources based not on economic efficiency but to channel it in ways sought by the state. Strong elements of financial repression continue to be in place: *e.g.*, the lack of a properly functioning bond market; forced government bond investments by banks, insurance companies and pension funds; directed credit; specialised financial institutions catering to the goals of policy makers. All these dimensions derive from financial repression. Epiphenomena such as flaws in competition policy, segmentation and barriers to innovation, are rooted in this deeper system of appropriation by the State of financial resources.

2.2. Capital controls

Flaws of competition policy, segmentation and barriers to innovation have been enabled and perpetuated by capital controls. As has been seen in India's real economy, if foreign financial service providers were able to bring genuine competition to bear against local firms through unrestricted entry, this would rapidly change the behaviour of local firms and of policy makers.

2.3. Autarky

Flaws in competition policy, segmentation and barriers to innovation have been enabled and perpetuated by an autarkic mindset that favours Indian firms at the expense of foreign firms in a manner considered so routine and 'natural' that the counterview is deemed unpatriotic.

The provision of IFS from an IFC is uncompromisingly *international*. The players, the regulator and the legal framework have to be designed for global participation and competition, avoiding the traditional instincts of falling back into autarky. Indeed, in GFCs, an autarkic mindset would be opposed by *national* financial firms. Box 10.1 shows a fascinating example of the thought process at the US CFTC on the relationship between trading in the UK and trading in the US.

India's experiment with autarky from 1947 to 1973, where the trade/GDP ratio fell from 17% to 8% is well known to be a failure. From 1973 onwards India has been reintegrating into the world. At first, the trade/GDP ratio rose slowly, returning to the 17% level only in 1993. In recent years, the growth of trade has been more frenetic. The trade/GDP ratio has risen from 20% in 1999 to 30% in 2005. This growth of trade in goods has been exceeded by growth of trade in services. India has made significant progress on reintegrating into the world economy since 1990. Yet, policy-making in too many areas remains dominated by an autarkic ethos. This is clearly manifest in the degree of protectionism in finance. While far-reaching trade reforms have taken place, and India is now perhaps two to three years away from ASEAN-quality trade barriers, foreign firms continue to be barred from operating freely in numerous parts of Indian finance.

As Table 10.1 above shows, global IFS is dominated by a small number of important global firms. Nearly 73% of global currency trading is accounted for by just 10 firms. India has many good financial firms. Realistically, no Indian firm is going to break into this top-10 ranking in the next decade. But in the following decade it is entirely possible that an Indian financial firm may be able to buy or merge with one or more of the global big ten. The bulk of jobs created by an IFC in Mumbai will almost certainly be created by foreign financial firms. Hence, for Mumbai to become an IFC, it is absolutely essential that key global financial firms consider Mumbai as a location to shift their IFS business to.

For Mumbai to become an IFC that can eventually compete with GFCs, the policy goal has to shift away from championing the immediate short-term interests of Indian firms and shareholders to championing the interests of Indian employees. Too often, the discourse between the Indian governance regime and global financial firms has been one where India has tried to prevent global financial firms from participating in India. For Mumbai to become an IFC, that legacy will need to be reversed. All the arms of the Indian state should seek to attract participation by global financial firms in India for the export of IFS. That may require opening up its market for domestic financial services. While Indian financial firms may resent that competition, as in the real economy, they will be better off in confronting it and so will the Indian consumer.

This change would be similar to that which has taken place in manufacturing – where India once tried to block foreign

Table 10.1: The role of the largest firms in global currency trading, May 2005

	Firm	Share in total volume (%)
1.	Deutsche Bank	17.0
2.	UBS	12.5
3.	Citigroup	7.5
4.	HSBC	6.4
5.	Barclays	5.9
6.	Merrill Lynch	5.7
7.	JP Morgan Chase	5.3
8.	Goldman Sachs	4.4
9.	ABN Amro	4.2
10.	Morgan Stanley	3.9
	All other firms put together	27.2
	Total	100

Source: IFSL, `http://tinyurl.com/yzg4mj`

Box 10.1: *Internationalisation of financial regulation: an example*

As electronic trading platforms and cash settlement allow derivative contracts on anything to be traded anywhere in the world, the principle of 'local regulation of local markets' has become difficult to apply. Where is a financial market located when it operates in the ether? Is it the jurisdiction in which the exchange chooses to locate its computers? Or do we have to consider the nationality of the owners of the exchange or the nationality of those who trade on the exchange or the location of the principal cash market for the underlying contract?

A recent example highlighting the importance of these questions is the ability of the US based Intercontinental Exchange (ICE) to offer US energy contracts to US investors through its own terminals without attracting US regulatory jurisdiction – thus benefiting from the principles-based regulation of the UK. ICE Futures in London (formerly the International Petroleum Exchange or IPE) which is owned by ICE, launched futures on the WTI crude oil that is consumed in the US, as opposed to the Brent crude futures that is normally traded in London. These are cash settled off the WTI price in the US (at NYMEX). After ICE was permitted to use its trading terminals in the United States to allow US investors to trade the WTI crude oil futures on ICE Futures in London, WTI volumes in ICE Futures have grown to about half of the NYMEX volumes. The result is a fascinating situation where there is:

1. A liquid contract on a US commodity
2. It is predominantly traded by US participants
3. It uses terminals in the US
4. It is traded on an exchange that is owned by a US entity
5. But it is located and regulated in the UK for reasons of regulatory arbitrage.

After the collapse of Amaranth, a large US hedge fund that had huge positions in energy futures both in ICE and in NYMEX, the US Commodities and Futures Trading Commission (CFTC) reviewed and reaffirmed its existing policy exempting the ICE futures contract from US regulation on the ground that it is a contract on a foreign exchange. The CFTC stated that:

1. The trading volume originating in the US did not determine a US location
2. The fact that the contract is based on a US produced or economically important commodity did not probate location

The CFTC will thus continue to rely on the quality of the regulation of ICE Futures by the UK Financial Services Authority (FSA) as well as the information sharing arrangements that it has with FSA. This thinking by the CFTC underlines a mature and internationalised perspective on financial regulation, uncontaminated by nationalist pressures or resentment about 'regulatory arbitrage'.

If Indian regulators accept the principles followed by the CFTC, foreign exchanges would be able to offer their contracts directly in India through electronic trading platforms. This would not require full capital account convertibility since the RBI now allows Indian citizens to remit up to $50,000 a year outside India for investment purposes. Indian citizens can use this facility to pay for the contracts that they buy on foreign exchanges. Foreign exchanges would also be able to offer trading in India on ADRs and GDRs of Indian companies provided the Indian investor pays for them in dollars. This would produce better price discovery in the ADR market and reduce the price gap between the Indian and offshore markets.

Source: Blog entries by Jayanth Varma, `http://tinyurl.com/yz6b7`

firms but now engages enthusiastically in promoting inward FDI for export-oriented manufacturing firms that can also supply the domestic market. India has replaced its legacy of autarky with an open economy when it comes to trade in goods and most services except financial services. Teams of Indian workers are tightly integrated into the world economy when it comes to BPO which has yielded $20 billion of export revenues. Such phenomena are starting to take place in manufacturing also. A comparable philosophical change is now required in the finance industry, if India is to achieve $40–50 billion of export revenues in finance and, alternatively to prevent the drain of $50–70 billion in payments for IFS acquired abroad. A serious effort to create an IFC will involve road-shows all over the world where presentations are made to global financial firms requesting them to consider India as a destination for FDI in finance. Export-orientation in finance requires attracting FDI exactly like export-orientation in manufacturing does.

2.4. Legacy institutional architecture

The problems of competition policy, segmentation and barriers to innovation that inhibit Mumbai's emergence as an IFC are partly the consequence of a financial regime governance whose foundations were designed at a time when the world of finance, the functions of regulation, the contours of financial activity, and global competition in IFS, were different.

While the superstructure of this governance regime has been modified in bits and pieces from time to time to yield a shape of multiple regulators that is distinctly ungainly in design and, perhaps dysfunctional, the conceptual foundations of the basic regime have remained untouched. The RBI Act was first drafted in 1934. Although it has been amended several times since it has not been fundamentally changed at its roots. The SC(R) Act was drafted in 1953 and the FC(R) Act in 1952. The separation between SEBI and FMC is rooted in the FC(R) Act of 1952. The strategic thinking governing these three Acts would be addressed very differently if they were to be drafted using contemporary knowledge.

Many of the problems of competition policy, segmentation and barriers to innovation that India's financial system confronts, and that impinge heavily on the issue of making Mumbai an IFC, flow from the conflicts of interest inherent in the multiple objectives and activities of the RBI, ultimately derived from the original RBI Act. In addressing the problems of competition policy, segmentation and the barriers to innovation in finance, the roles, functions, attitudes, ethos and objectives of financial regulatory agencies in India requires a new look; particularly in light of what has been happening in the world as well as the different realities of 21st century India.

3. Deeper sources of dysfunction

It would be misleading to suggest or conclude from the foregoing discussion that the several complex issues raised by financial regulation in India, are issues purely of regulation ***per se***. They often have more to do with the legacy context in which financial regulation has evolved to accommodate an array of multiple objectives – both regulatory and strategic. These often conflict; implicitly if not visibly. In that connection, it should be noted that a considerable burden has been placed upon the RBI for taking the brunt of dealing with continuing difficult structural adjustment since 1992. The weight of adjustment has fallen disproportionately on adjusting monetary and exchange rate policy simply because fiscal policy has proven stickier, and insufficiently elastic/flexible, in adjusting commensurately, for reasons of political economy. In performing this task, RBI has also had to protect: (a) the soundness of the Indian financial system, as well as (b) the government's interests as India' single largest shareholder in financial firms.

The adroit manner in which that dual responsibility has been acquitted is not as fully realised or appreciated as it should be. Many astute observers of the financial scene believe that such a doctrine – which derives from the authority of a reputation earned and acknowledged over a long period of time – is now being exercised in a manner that continues to protect the contours of financial regime governance from an era of autarky that has now passed and become dysfunctional.

In doing so, it is implicitly influencing the future development of the Indian financial system (inadvertently or otherwise) in ways that may not necessarily be consonant with Mumbai becoming an IFC or with Indian firms competing effectively for providing IFS in the global arena. With the inhibitions and restrictions leading to financial repression (or inadvertent implicit suppression of innovation) having their roots in deeper historical realities that have not yet adapted to the agenda for reform, it is necessary to be clearer about what these realities actually are, and what needs to be done to alter them, to enable India's evolution as one of the world's most significant economies to occur as smoothly and painlessly as possible.

3.1. The 'ownership' problem and the conflicts-of-interest it causes

As in China, **government ownership** continues to be a major feature of India's financial system. It poses the same difficult challenges for both these countries as they attempt to export IFS and globalise their financial systems. There is now universal agreement, in global academic and financial circles, that public ownership of financial firms creates an intractable number of avoidable difficulties in influencing the development and regulation of sound financial systems. Most importantly (in the context of the emerging Basel-II regime), a number of conflicts-of-interest arise between the roles of government as the ultimate **apex regulator** of the financial services industry (which it remains in the absence of constitutional independence and legal/juridical separation from government of the RBI, SEBI, FMC, and other regulators) while also being:

(a) The **largest owner** of financial firms being regulated: *i.e.*, commercial banks – and their capital markets subsidiaries – as well as in other parts of the financial services industry such as: specialised long-term financial institutions, insurance companies, asset management firms, pension funds, and firms/agencies involved in commodities.

In the mutual funds industry (and, to a lesser extent, insurance), India has made some progress with permitting entry of private and foreign players, as well as creating a more level playing field in regulating that industry. The point has now been reached where, although UTI is still the dominant mutual fund, it no longer commands an overwhelming market share.

For Mumbai to become a viable and competitive IFC within the next few years, this successful experiment in the asset management segment of financial services, needs to be replicated in all other segments, most particularly banking and insurance. It needs to be accompanied by eliminating restrictions on: (i) the formation of financial conglomerates or LCFIs that can compete with their counterparts in the rest of the world; and (ii) the entry of hedge funds and the entire range of other funds such as exchange traded funds across the spectrum.

(b) The **single largest borrower** from the Indian financial system, with an inherent vested interest in keeping the cost of its borrowing suppressed to the extent possible; even when that might have larger implications in managing monetary policy and sending signals through interest rates that affect every big price in the economy.

In the absence of constitutionally guaranteed regulatory independence – *i.e.*, with regulators being independent public agencies accountable to the legislature (as they are in many countries) rather than to government – the government's ultimate responsibility for sound, impartial and objective regulation, collides unavoidably with its ownership and borrowing interests. Not only does that create a conflict of interest in a fundamental sense (*i.e.*, the *non sequitur* that arises from an entity regulating itself), it also incurs the risk of compromising fairness of treatment on a uniform basis for all financial firms.

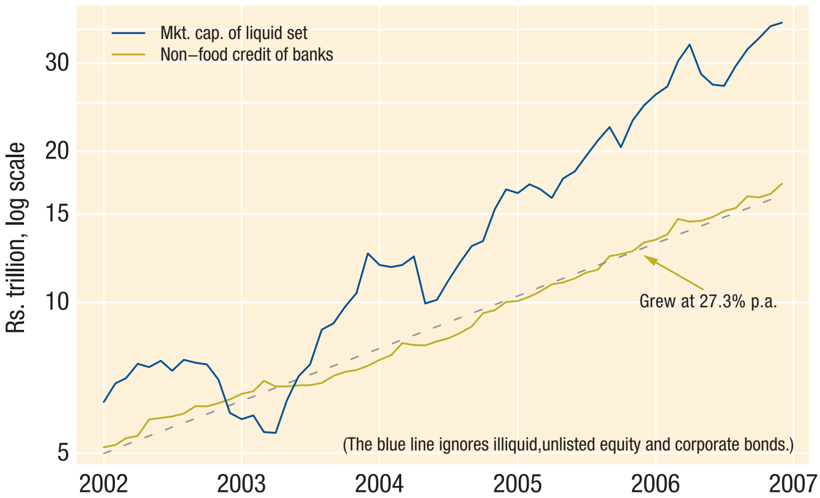
Apart from the invidious and corrosive nature of these conflicts of interest, studies of government ownership of financial firms around the world suggest that it leads to a normal propensity to protect, at any cost, the survival and profitability of public sector financial firms through artificial means. By so doing, it generates perverse incentives for government to diminish competition, enforce artificial and counterproductive segmentation, and throw up greater barriers to innovation.

In evaluating the characteristics of established or emerging IFCs worldwide, it is significant that none of these cities (other than Shanghai, which is further behind than Mumbai in having a financial services industry that can become globally competitive quickly) have any significant public ownership of financial firms in any segment of financial markets. The most vibrant parts of Indian finance – the securities markets – where export competitiveness is perhaps most visible in the attraction of voluminous foreign portfolio investment, are the parts where public ownership is the smallest. That is no mere coincidence. It signals clearly what the government needs to do in withdrawing gradually but resolutely from the ownership of all financial firms within the political economy constraints it confronts (but not using those as a reason to defer taking action indefinitely). That is indispensable to create the institutional and competitiveness conditions that are necessary and fundamental for Mumbai to become a viable IFC.

3.2. Strategic issues of public debt financing and management

An in-built propensity toward financial repression has become chronic and endemic in India. It has its origins in historical conceptual notions among post-independence policy-makers, seduced by the supposed development success of the USSR in 1918–50, about how public (sovereign and sub-sovereign) debt should be financed and managed. Lacking belief in the efficacy, desirability (and feasibility) of India's having efficient capital markets in the 1950s, the option of creating a wide, deep and open bond market (for sovereigns, sub-sovereigns, municipals and corporates) – of the kind that now characterises almost all mature economies – was eschewed in the nascent stages of India's economic and financial system development.

Figure 10.1: Market capitalisation of COSPI firms against non-food credit (trillion rupees)



In the 21st century there is a need for fresh thinking on the part of policy-makers about strategic issues of debt financing, issuance and management. Financial liberalisation does not inevitably imply that it will result in a shortage of voluntary and enthusiastic buyers for government bonds. Quite the contrary; whereas resident Indian investors with few portfolio diversification opportunities might be sated with Indian sovereign obligations, either directly or indirectly, global investors have an enormous appetite for digesting Indian paper that has not been addressed, leave alone satiated.

Through financial sector reforms, a liquid INR yield curve can easily be attained, with a market populated by a very large number of participants. This is likely to deliver superior, and far more flexible, financing options along the maturity/duration and coupon spectrum. It would also widen geographical scope for financing the fiscal deficit; especially in the global marketplace (even for paper denominated in INR) when compared with the present regime.

Resorting to the global marketplace, and meeting global demand for Indian sovereign paper, would ease crowding out pressures and pre-emption in the domestic market. That would have the benefit of easing demand-supply induced pressures on Indian interest rates. It would create more room for manoeuvre on the part of RBI in executing monetary policy; independent of the MoF view on what the level of interest rates should be. The lack of independence of the central bank hinders acceptance by global investors who prefer to operate in an IFC that adopts global norms concerning separation of powers between monetary and fiscal authorities, and permits independence on the part of both to pursue the most appropriate and optimal policy options.

A key part of this strategic thinking on debt management is the role of foreign investors. A liquid INR yield curve that can be traded in an efficient bond and bill market by foreign investors is likely to attract enormous investment flows into Indian sovereign debt from long-term global fixed income portfolios like pension funds. This would result from (a) pressures for diversification in global fixed income portfolios, especially favouring investment in developing economies that can sustain a superior growth rate over several decades as India can, providing its real economy is managed as well as it is now and its financial system reflects global standards; and (b) the positive outlook for India and the INR over the next 20–30 years. The participation of these investors requires a modern bond market. That feeds back into establishing a liquid INR yield curve. Access to such financing would constitute a far-reaching transformation of Indian public finance.

3.3. Lack of strategy on the transition from a bank-dominated system toward a market-dominated financial system

Finally, there has been an absence of sufficiently clear strategic thinking on the evolution of finance, both domestically and internationally, away from banking towards securities (Litan, 1991). In India, an examination of the liabilities of firms on a market value basis shows the dominance of equity financing. As shown in Figure 10.1, the market capitalisation of the top 2,500 firms of the equity market stands at roughly twice the size of non-food credit of the banking system (which comprises loans delivered to big companies, small companies and individuals).

A commensurate transformation of the policy framework has not taken place. In many respects, Indian finance continues to be rooted in the past, with a banking-dominated financial system that should, by now, have become much more capital-market oriented especially in the market for debt in the form of traded securities rather than bank loans.

4. What impedes Mumbai from becoming an IFC? A summary

This group of three chapters has dealt with some of the critical hurdles that presently impede the emergence of Mumbai as an IFC. Clearly, making the profound changes that are necessary in financial regime governance (*i.e.*, adapting legislation to meet modern realities, policy-making, regulation, enforcement, and changes in the functioning of the legal system that provides recourse for contractual dispute settlement) is a complex undertaking. Swift progress will be difficult to make.

India has a reputation for taking far too much time to contemplate and discuss changes *ad infinitum* without necessarily acting on them. China has the opposite reputation of acting too swiftly, without thinking through all the implications.

So far China has made more progress than India.[1] Perhaps there is a lesson in there somewhere, although the optimal solution would be to blend both these opposite tendencies in a happy medium. Neither country can afford, however, to delay its entry into the burgeoning global market for providing IFS – driven in large measure by their own needs as they become more significant players in the global economy. The Indian financial industry and policy-makers need to focus on, and engage with, these problems at many levels simultaneously, in order to address these difficulties.

Portraying the world of IFS in a somewhat simplistic but nevertheless powerfully illustrative matrix, the wallchart constructed for this purpose offers specific, tangible views on what holds back a specific IFS from being provided in India and what needs to be done to make India a significant player in IFS markets on the world stage.

[1]See `http://tinyurl.com/yu4zk7` on the web on this theme.