NORTH MACEDONIA

Less is More Consolidation of the Macedonian Banking Market Improves Competition

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The main characteristics of the Macedonian banking market are its small size and the relatively large number of players. According to the latest reports of the National Bank of North Macedonia, out of fifteen active banks, five have significantly higher market shares than the rest. The combined market share of these five biggest banks is 74.4%, with a significant discrepancy between the bank that owns the largest amount of assets (a market share of 22.7%) and the one with the lowest (a market share of 0.5%).

In respect to the assets owned, eleven active banks majority-owned by foreign shareholders have a combined market share of 71.1%. The highest market share of these foreign-owned banks – 79.9% – is in the segment of loan activities.

According to the National Bank's Quartal Reports for 2017 and 2018, competition among banks, based on the Herfindahl-Hirschman Index, is shrinking. Indicators of the level of competition are the number of market players and the quantity of their market share. Due to the large number of banks with a small market share, the Macedonian banking market qualifies as a non-competitive environment.

Many believe that a non-competitive environment is not good for a country's economy, as a competitive banking market lowers costs and extends the products portfolio for consumers and stimulates the banks to innovate. Thus, it comes as no surprise that the EBRD has highlighted the consolidation of the banking market as a priority in its Transition Report for North Macedonia 2018-19. The main benefit of the proposed consolidation would be a strengthening of the market, which should enhance the flow of goods and services in the country's economy.

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The need for consolidation of the banking market has been recognized by the National Bank of North Macedonia as well. The Governor of the Bank, Anita Angelovska-Bezoska, has stated that lowering the number of banks should increase competition in the market, thereby expanding the portfolio of products offered by the banks.

It is left to the National Bank of North Macedonia to determine the most appropriate measures to take in consolidating the banking market. In preparing its strategy to build up the national banking market, the National Bank will have to consider best practices in other countries, as well as the specifics of the Macedonian market.

The Bank must be careful, as the stability of the banking market is crucial and any instability may spread by contagion to the whole economy by distorting the interbank lending market as well as credit availability and could ultimately lead to recession. Some characteristics of the banking market, such as tight regulations, entry barriers, and strict supervision, differentiate it from other traditional markets. Therefore, the manner of encouraging competition within the banking market should be adjusted to its characteristics.

The most compelling argument for consolidating the banking market is the fact that larger banks are able both to diversify risks and utilize the economy of scale to reduce costs by increasing the size of the business. Studies show that less-competitive banking markets can be costlier and exhibit a lower quality of services, with a consequent reduction in the effective demand for external financing and discouraging economic growth.

On the other hand, other studies emphasize that in a non-competitive banking environment banks can form long-term relationships with borrowers and lend more, with a lower interest rate, than banks in a competitive environment, due to their belief that they will be able to extract a large portion of the future surplus of the borrowers.

It is obvious that theory alone is unclear about the consequence of reducing the number of banks and increasing competition in this market. As a result, the consequences of the consolidation and increase of competition in the banking market in North Macedonia will need, ultimately, to be assessed empirically, by using both theory and best practices from elsewhere in the EU.

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