

REVIEW OF BANKING PERFORMANCE IN REPUBLIC OF NORTH MACEDONIA DURING ECONOMIC DOWNTURNS: EXPECTED OUTCOME FROM COVID 19

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ABSTRACT

The main role of the banking system is to enable entities with excess financial resources to invest and transfer to entities that lack financial resources (and have sustained plans for new projects), with the ultimate goal of making a profit. Recessionary tendencies in the world economy, as well as the slowdown in domestic growth are negatively reflecting on the financial capacity of enterprises and their ability to regularly service liabilities. These problems in the corporate sector spill over into the banking sector over certain time delay, decreasing the bank's profitability and efficiency as well as rising its vulnerability.

After the global financial crisis 2007-2009, which made significant impact on the banking industry, new adverse macroeconomic conditions emerge globally due to COVID 19 pandemic. For a short period of time the lockdown caused a collapse of financial markets, breakdown of global value chains, and restrictions in financial flows in general.

Thus, the purpose of this paper is to analyze the performance of the Macedonian banking sector during the last financial crises, regarding its profitability and risk profile, and compare them with the recent banking performance indicators, so to derive assumptions: if the lockdown caused by COVID 19 would affect the performance of the Macedonian banking sector. In this research, secondary data are used regarding particular indicators for banks that are offering services on Macedonian territory. These data will be additionally analyzed and described by conducting comparisons for different time periods and for different group of banks. The results from the analysis show that the banking sector won't be immune to the impact of the unfavorable economic conditions, but the intensity of the decline in their performance will be directly under the influence of the operating efficiency of bank management. Large banks, because of their high value of operating efficiency, stable deposit base and more effective embedded systems for risk management will be more resilient to this turbulence.

KEYWORDS: bank's performance, bank's profitability, credit risk, liquidity risk, solvency, NPLs

JEL CLASSIFICATION CODES: G21, G01

1. INTRODUCTION

The role of banks is dominant in financing economic activity and the effectiveness of banking sector has positive impact on economic growth. According to (Athanasoglou et al, 2005) sound and profitable banking sector is better able to withstand negative shocks and contribute to the stability of the financial system. Profitability and stability are crucial indicators of banking system health. A profitable banking sector is better able to withstand negative shocks and contribute to the stability of the financial system as a whole. Therefore, many academic researchers, bank managers, investors and supervisory bodies pay special attention to the bank's performance, expressed in terms of profitability and risk profile. The

main purpose of their research is to discover the determinants that most affect the banking sector performance.

Most of the empirical researches which have been developed are considering the banks' performance in developed market economies. For example, Berger (1995) in his research, conducted for a sample of US bank for period 2000-2007, finds positive relationship between the bank performance and the capital to asset ratio. Athanasoglou et al. (2008), investigate different groups of factor, which affect bank's profitability, such as macroeconomic, bank-specific and industry-specific determinants. The key finding was that all bank specific determinants, with the exception of bank size, have significant impact on bank's profitability. Li (2007) measures the impact that certain risks, such as credit, liquidity and solvency risk and macroeconomic conditions have on bank's profitability in the UK banking industry over the period of 1999 to 2006. His research concludes that credit risks have a statistically significant impact on bank profitability, i.e. higher credit risks results in lower profit; and additional determinant on bank's profitability with strong statistical significance is the capital strength.

Afanasieff et al. (2002), as a representative of studies, which focus on bank's performance in emerging economies, finds that macroeconomic variables are the most significant determinants of bank interest spread in Brazil. Flamini et al. (2009) conducted a research of a sample of 389 banks in 41 countries in Sub-Saharan Africa and find that apart from credit risk; higher returns on assets (ROA) are associated with larger bank size, activity diversification, and private ownership. Bank returns are also affected by macroeconomic variables, suggesting that macroeconomic policies that promote low inflation and stable output growth do boost credit expansion. That is why macroeconomic stability with low inflation and stable economic growth is essential for a healthy financial system.

The performance of banking sector especially attracted more attention during the recent global financial crisis that originated in the US and spread throughout the world, causing long-term problems for the banking sector. It has been shown in the literature that financial crises have a significant and even permanent effect on economic growth. Specifically, by destabilizing the financial sector, financial crises affect the performance of the real economy through reducing the availability of credit and increasing uncertainty about future gains, and thus decreasing the level of investment and consumption. A key potential contributor to the performance of banking sector is the financial crisis itself, in the form of a negative shock to the much needed supply of external finance. This suggests that the performance of banking sector and the developments in the real economy, as macroeconomic determinants of banks' performance, are strictly related.

Another key point for discussing about the macroeconomic determinants of bank's performance is that, when the national economy faces an economic boom and banks are profitable with proper capital adequacy, non-performing loans are low and stable. However, during economic downturns non-performing loans are the most vulnerable category. Furthermore, according to the analysis conducted by Nikolov and Popovska-Kamnar (2016), shows that non-performing loans are results of macro and bank determinants and that the decline in economic activity in the country contributes to asset deterioration of banks and an increase in non-performing loans. The increase in non-performing loans and the impairment of problematic loans has great impact on bank's risk profile and solvency position. This results in refraining the bank from lending (because of reduced consumption and failed companies), which further reduces economic activity and this reduced economic activity causes a larger amount of non-performing loans. In this way, one can note that a spiral can be created, which is harmful for the performance of the banking system and the economy as a whole. From this point of view, loan portfolio with reduced quality and reduced credit demand can cause low profitability, reduced liquidity and solvency.

“Non-performing loan may have effects such as: reducing market confidence in the bank, increasing its reputational risk and contributing to depositors withdrawing their deposits or increasing funding costs. Also, a high amount of non-performing loans is one of the main reasons for systemic insolvency of the banking sector, which presents a threat and obstacle not only to the development of the banking system, but to the economic system as a whole.” (Jolevski, 2017, pg.6)

Expecting that more efficient banks will be more profitable and stable, and more resilient during economic turbulence, Mirzaei (2013) investigated the bank performance determinant for 6540 banks in 49 emerging and advanced economies during the crisis period 2007–2010. His results showed that efficient banks perform better.

Given the fact that macroeconomic instability has significant impact on banking sector performance, this paper analyzes the effects that the last financial crisis had on Macedonian banking sector performance, in order to make certain statements about the condition of banking sector and to derive assumptions about the impact that COVID 19 will have on the performance of Macedonian banking sector. Firstly, by analyzing the profitability and risk profile of the banking sector with additional explanations regarding the causes, this paper will provide an overview of Macedonian banking performance. Second, it reviews the performance of separate group of banks during the period of 2007 to 2019, for the purpose of determining characteristics for each, third it gives a brief explanatory regarding the measures that NBRNM introduced for handling with the corona crisis, and finally, it offers conclusions tied to the future performance of Macedonian banking sector as a result of the impact that corona crisis has.

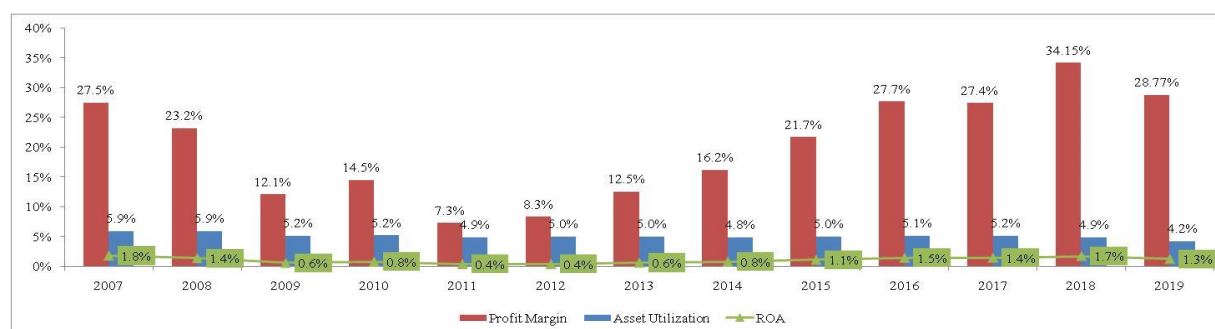
2. REVIEW OF BANKING PERFORMANCE IN REPUBLIC OF NORTH MACEDONIA

The Macedonian banking system was not directly affected by the world economic crisis in 2008, but it could not avoid the indirect effects of the global economic crisis that was spilled over the domestic real sector. The stable financial condition of our banking system was derived from its "closure" to international financial markets, the non-existence of exposure to the so-called "toxic products", its relative strong capital and liquidity position, caution when taking risks, as well as macro prudential measures taken by the National Bank. Still, due to the global economic turbulence, the performance of the Macedonian banking sector was visibly deteriorated in 2009, one year later after the Global Financial Crisis.

The successful performance of banks measured by return on assets (ROA) shows the bank's ability to use financial and material resources in a way that will ensure the highest possible earnings. Banks' profitability is represented here by return on average assets (ROAA) on figure 1, and has its greatest declines in 2009 and 2011. The main factors that contributed to this reduced profitability by Macedonian banks can be derived by using the Du Pont Formula. According to Du Pont Analysis, the formula for calculating ROAA can be broken down in two parts: profit margin and asset utilization.

The Profit margin, calculated as a ratio between the net-income and total revenues, acts as an indicator of a bank's effectiveness in cost control and in generating revenues. In figure 1, the profit margin in 2009 and 2011 has its lowest values, 12.1% and 7.3%, respectively. According to the data presented to the National Bank by the Macedonian banks, the cost to income ratio in 2009 and 2011 is 70.1% and 67.8% respectively, and it shows that operating expenses were sharply increased. The increase of operating expenses, and the decline in net profit margin, was mostly due to the deteriorating quality of loan portfolios, and the increase of provision for loan losses. Additional factors that contributed to the decrease of the profit margin in the banking system were: the decreased rate of growth of bank activities, especially the credit activity, which was reflected in the decrease of the net-interest income by 5.8% and the intense competition in the banking market for sustaining a stable deposit base which increased the passive interest rates and created an additional raising in operating expenses.

Figure 1 ROAA - profitability indicator of the Macedonian Banking Sector



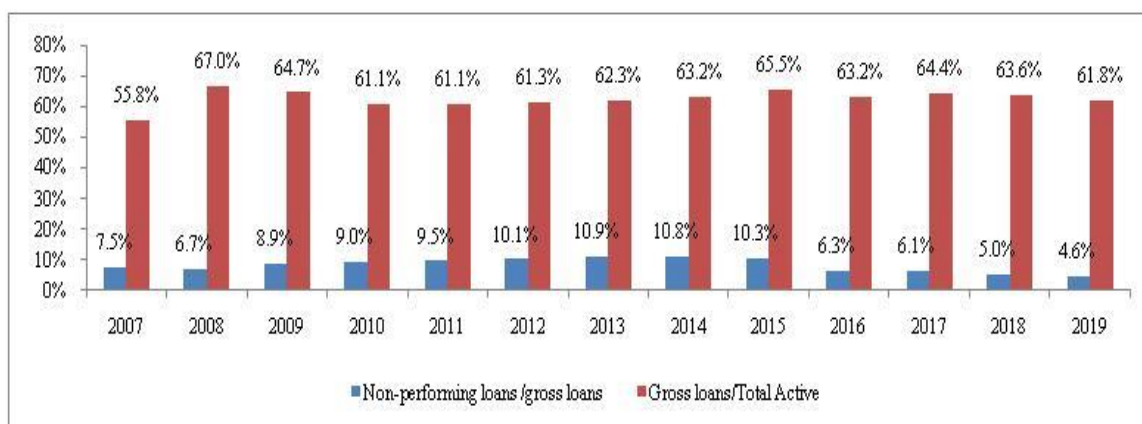
Source: Own data processing according to Banking system indicators publicly available on: http://www.nbrm.mk/bankarska_supervizija_i_rieghulativa-en2.nsp

Asset utilization, calculated as a ratio between the total income and total assets, reflects the bank's management efficiency in investing in different types of assets which have different yield interest. In 2009, the Asset utilization has a value of 5.2%, and this lowered value comes as a result of the increase in the total assets and decrease in total income. However, the growth in total assets came as a result of the increased share of cash and balances at the National Bank, and the placements at domestic and foreign banks. This increase of cash and balances at the National Bank was a result of legislation changes regarding the calculation and meeting the reserve requirement of banks. In 2009, there was also an increase in the placements in banks, mostly as a result of the introduced obligation (in December 2008) for banks to achieve minimum liquidity rates prescribed by the National Bank. Analyzing the total income in the banking sector, one can note that its growth rate declined, but mostly due to the decrease in the credit demand, i.e. the sale of loans, especially to the corporate sector. In disrupted economic flows, the corporate, and household sector sustain from investment activity. Therefore, banks' management teams decide to invest their available funds in securities in order to overcome the loss from net interest income.

The risk profile of the Macedonian banking sector is analyzed by using several indicators of credit, liquid, and solvency risk. In addition, the analysis of risk profile of the banking sector starts from credit risk, because it plays a crucial role in the arising problems in all areas of banking operations, such as liquidity or the usage of capital for covering credit losses.

Credit risk, or risk of default, is a subject to numerous theoretical and empirical researches, and many of them connect credit quality of loan portfolio with economic activity. Generally, credit risk is associated with the traditional lending activity of banks and it is simply described as the risk of a loan not being repaid in part or in full. The rising share of non - performing loans (NPLs) in total loans in the banking sector is one of the biggest problems in economic stagnation. According to the IMF, this ratio is a backward-looking indicator, which means that NPLs are identified when problems already emerged. Furthermore, according to Demircuc-Kunt and Detragiache (1998), the banking crisis is defined as a crisis when the NPLs/Total loans ratio is above 10% and that it is an alarming signal for higher bank exposure to risk. As shown in figure 2, the greatest increase in the share of NPLs occurs in 2009, and looking further in 2010 and 2011, there is only a slight increase to 9.5%, but the share of gross loans in total active has decreased from 2009 and onwards to 2012, when its value remains constant at 61%. These two indicators show a decline in the credit activity of the banking sector with a simultaneous increase in the NPLs. The banking sector reduced its credit activity, due to the reduced credit demand, and the increased share of NPLs. According to the data presented by NBRNM (2012) movements of total non-performing loans arise from the variable movement of non-performing loans in the corporate sector. They are main driver of nonperforming loans with a share of around 80% in the total non-performing loans.

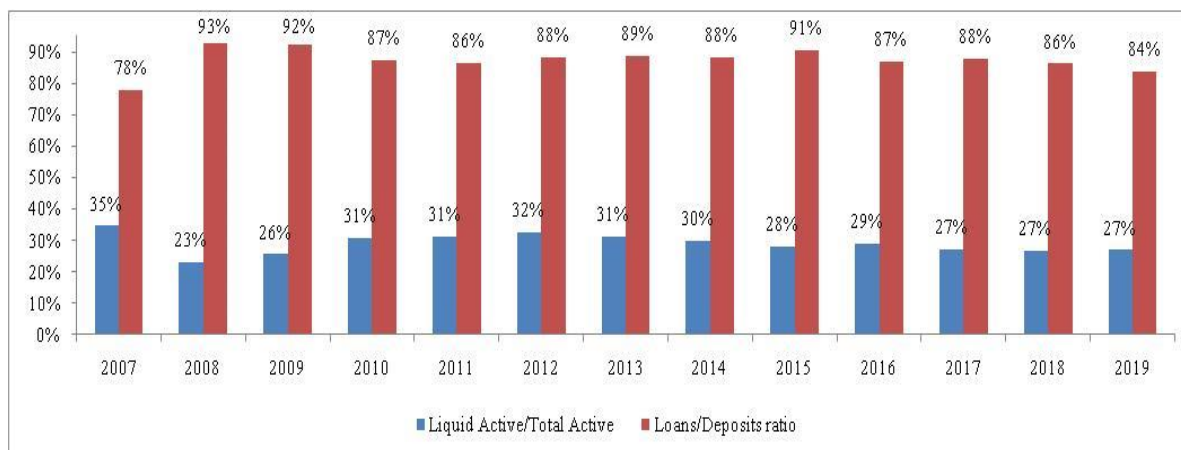
Figure 2 Credit risk indicators



Source: Own data processing according to Banking system indicators publicly available on: http://www.nbrm.mk/bankarska_supervizija_i_rieghulativa-en2.nsp

The banking sector in RNM is characterized with low liquidity risk. The share of the liquid active in the total active has its greatest rate of growth in 2009 and 2010 (as shown in figure 3), when the banking system notes reduced share of gross loans in total active, but also high share of investment in treasury bills and government securities.

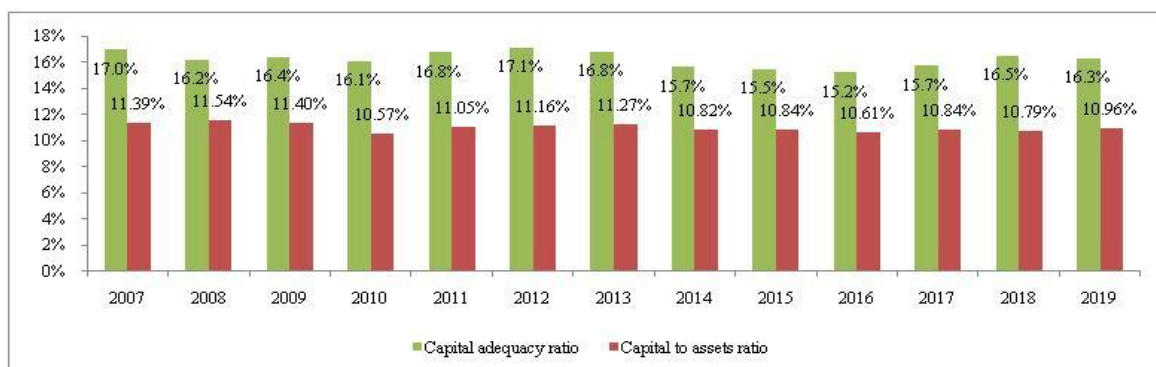
Figure 3 Liquidity risk indicators



Source: Own data processing according to Banking system indicators publicly available on: http://www.nbrm.mk/bankarska_supervizija_i_rieghulativa-en2.nsp

Banks were directed towards investing in assets that are easily converted into cash, apart from investing in loans, which represent the least liquid bank asset. Further, loan to deposit ratio, expressed in percentage shows whether banks have enough liquidity to cover any unforeseen fund requirements. If a bank finds itself with too few deposits to fund loans, then it must rely more heavily on non-deposit sources of funds, whose availability and price are much more sensitive to changing economic or financial conditions. So, if these non-deposit sources of funds become more expensive or dry up, the bank will weaken its financial health and even threaten its viability. According to practitioners, a good loan to deposit ratio ranges from 80% to 90%, and the Macedonian banking sector has a solid liquidity.

The risk of solvency as an inability of banks to meet their long-term debts and financial obligations is measured as a ratio between the banks' capital and total assets. Two types of indicators are shown on figure 4, because of the possibility for complementary analysis. The capital adequacy ratio (CAR) actually shows the available capital of banks in relation to overall risks they face. It is an especially important indicator that regulators track to ensure that the banks can withstand significant – but not unreasonable – losses or fluctuation in revenues. The primary function of CAR is to effectuate efficient and stable financial systems. It indicates the extent to which assets are funded by other than own funds and is a measure of capital adequacy of the deposit-taking sector. The capital to assets ratio as an indicator of banks' capital adequacy shows the financial leverage. The rationale behind this indicator is that if the market value of a bank's total assets is lower than its obligations, then the bank is insolvent. The proper capitalization of banks enables them to absorb the losses and to reduce the solvency risk. Solvency and capitalization of the banking system remained high during the Global Financial Crisis and even improved due to the higher growth rates of capital positions of the banks compared to the growth rates of the banking system activities (risk weighted assets). Our banking system is characterized with continuous high quality of capital positions, mostly due to the increase in Tier I capital. Additionally, the latest results from stress testing (simulations from the NBRNM) at the end of 2019, show that despite the high increase of non-performing loans, the CAR will not be under 8%. If 15.3% regular credit exposure transfer to non-performing credit exposure, then the capital adequacy of the banking system can be reduced to 8%.

Figure 4 Solvency and capitalization indicators

Source: Own data processing according to Banking system indicators publicly available on: http://www.nbrm.mk/bankarska_supervizija_i_riehulativa-en2.nsp

By reviewing the indicators of the banking sector's performance during and after the Global Financial Crisis, we can derive the following:

1. The operational capability of banks to generate revenue that cover operating expenses, started enhancing from 2013 onwards. At the end of 2019, the net profit margin of Macedonian banks was 29%, and it was especially under the influence of increased non-interest revenues. The credit activity of banks was normalized after 2012, when they were able to focus on diversifying their portfolio of banking activities and providing additional sources of income, offering wide range of financial services, e.g. bancassurance. Today, when facing the COVID 19 crisis, the banking management in RNM is efficient in the usage of the banks' profit-generating assets.

2. Due to the fact that credit activity is the core banking activity in the Macedonian banking system, the share of non-performing loans in total loans is one of the most significant factors with the greatest impact on bank's performance, especially in economic downturns. At the end of 2019, the Macedonian banking sector faced historically the lowest level of non-performing loans, which gives space for the banking sector to focus on efficient allocation of available funds towards creditworthy borrowers and restructuring of problematic loans.

3. During the period of global liquidity shortages, the liquidity position of banks in RNM was enhanced by the dominant role of domestic deposits as a source of funding, thanks to which the banking system did not face difficulties in providing sources of funding. As of December 2019, the Macedonian banking sector is characterized with high liquidity and high quality capital positions, but if there is a prolonged influence on the causes of profitability deterioration, in conditions of limited opportunities to provide new external sources for financing, there could be limited possibilities for increasing the capital position of banks from internal sources, through reinvestment of profit.

2.1. Review of banking performance by group of banks

The performance of the banking sector must be considered in terms of size of banks, due to their relatively different characteristics. Many studies deal with internal determinants of bank performance and use different variables such as size, equity capital etc. Akhavein et al. (1997) and Smirlock (1985) find a positive and significant relationship between size and bank profitability. Short (1979) argues that size is closely related to the capital adequacy of a bank since relatively large banks tend to raise less expensive capital and, hence, appear more profitable. Considering risk profile, during periods of increased uncertainty, financial institutions with poor asset quality and low levels of liquidity possess the two major causes of bank failures (Li, 2007). Davcev and Hourvoulides (2009) find out significant relationships between return on assets and return on equity ratios with the equity size, loan loss and operating expenses in the banks.

Large banks occupy the largest market share of banking products and services, have the widest network of branches, and are particularly active in international markets. Large banks in RNM have the largest share in total assets in the banking sector, i.e. their average share in total assets, for the observed period, is 62%. From aspect of profitability, return on equity and return on assets, large banks bounce off the

middle and small banks, even when the economy is slowing and growing negatively. Table 1 shows this trend.

Table 1. ROAA and ROAE as indicators of profitability – Large, medium and small size banks

	ROAA			ROAE		
	Large	Medium-	Small-size	Large	Medium-	Small-size
2007	2.0%	1.8%	0.1%	24.5%	12.1%	0.3%
2008	2.1%	0.2%	-0.7%	25.8%	1.2%	-1.5%
2009	1.3%	-0.5%	-1.3%	14.2%	-4.1%	-2.9%
2010	1.4%	-0.4%	-0.3%	15.5%	-0.7%	-0.7%
2011	1.2%	-1.1%	-1.0%	12.2%	-9.7%	-4.5%
2012	0.8%	0.2%	-5.6%	8.4%	1.7%	-39.3%
2013	0.8%	0.6%	-0.2%	7.1%	4.7%	-1.8%
2014	1.0%	0.7%	-0.6%	9.1%	5.5%	-5.5%
2015	1.3%	0.8%	-0.1%	12.5%	7.2%	-0.9%
2016	1.7%	0.8%	0.6%	16.0%	7.0%	5.2%
2017	1.7%	0.7%	-0.2%	16.5%	6.3%	-1.6%
2018	2.2%	0.3%	1.0%	20.4%	2.6%	9.6%
2019	1.8%	-0.4%	0.8%	16.1%	-3.4%	7.6%

Source: Own data processing according to Banking system indicators publicly available on: http://www.nbrm.mk/bankarska_supervizija_i_rieghulativa-en2.nsp

The negative or slow growth in the economy during the Global Financial Crisis, with the largest peak in the Macedonian banking sector in 2009 and 2011, negatively affected the profitability of large Macedonian banks. However, they did not report losses. The reduced values of ROAA and ROAE are reported til 2013, when their trend of increase begins. The reduced profitability of large banks, represented by ROAA, and indirectly through ROAE, results from the reduction of the profit margin by 10%, as a result of the greater growth of operating expenses from total revenues. This data can be supported by the cost to income ratio, which is an additional indicator of the bank's profitability and shows the relationship between the bank's expenses and revenues. This ratio gives a clear indication of how efficiently the bank works - the lower it is, the more profitable the bank is. The C / I ratio for large banks in 2009 increased by 8 percentage points (55.8%) and starts moving below 55% after 2011. The changes in this ratio highlight problems, ie costs grow at a higher rate than income. What is important to note here about large banks is that although the costs of the bank increases sharply, they significantly use the economies of scale and are more efficient in covering them. Medium and small banks report negative financial results during the Global Financial Crisis, but afterwards medium banks start showing positive tendencies of their profitability, while small banks are struggling to create high and stable revenues which will enable them long-term perspective for survival. Regarding the C/I ratio, one can note that medium and small banks have values above 70% which reflect their low operating efficiency.

Large banks in Macedonian banking sector are far more efficient in their operating by using economies of scale and they will be more resilient to the new economic turbulence Covid 19, but medium-size and, especially small banks should rethink or redesign their business model for the purpose of generating higher growth rate of revenues for covering expenses, or for increasing their efficiency. In terms of risk profile, ie credit risk, large banks have the largest share of gross loans in total assets, and they are most exposed to it. On the other hand, large banks are always characterized by a far better loan portfolio than medium and small banks, due to the better developed systems and credit risk management policy. Therefore, the share of non-performing loans in gross loans is lower compared to medium and small banks. While medium and large banks have a similar downward trend in the share of non-performing loans in total loans, small banks only after 2015 recorded such a significant trend. What is especially important to emphasize for the small banks, which in the Global Financial Crisis had about ¼ non-performing loans, they end 2019 with the lowest share of non-performing loans. This gives space for all groups of banks to focus on monitoring and control of already approved loans, with

appropriate proposals for their restructuring, as well as finding new lenders with high credit ratings in the following period.

In general, each group of banks has low share of NPLs in the loan portfolio, which indicates high quality of loan portfolios, and it is an excellent starting point for undertaking corrective and anticipated measures by banks for appropriate management of non-performing loans.

The liquidity risk of each group of banks is presented in the following table 2 through two indicators Liquid assets / Total assets and Loans / Deposits.

Table 2 Liquidity indicators by group of banks

	Liquid assets/ Total assets			Loans/ Deposits		
	Large	Mediu	Small-	Large	Medium-	Small-
2007	34.7%	36.6%	48.0%	75.8%	84.3%	75.1%
2008	21.1%	22.6%	55.1%	89.2%	105.0%	75.7%
2009	25.2%	23.8%	48.5%	87.1%	112.1%	73.8%
2010	30.1%	30.7%	47.6%	82.9%	103.4%	67.4%
2011	30.4%	29.7%	45.9%	83.1%	97.4%	79.1%
2012	31.5%	34.8%	30.4%	84.9%	96.4%	90.0%
2013	31.1%	31.2%	32.4%	83.2%	104.4%	86.7%
2014	33.9%	31.1%	33.6%	83.3%	104.8%	90.5%
2015	32.1%	29.0%	34.6%	86.2%	105.3%	89.6%
2016	32.0%	23.4%	34.9%	84.6%	98.6%	84.0%
2017	31.4%	21.3%	33.6%	84.4%	103.2%	84.4%
2018	32.4%	23.3%	33.0%	82.2%	103.2%	86.6%
2019	34.6%	23.2%	34.0%	78.5%	106.1%	89.5%

Source: Own data processing according to Banking system indicators publicly available on: http://www.nbrm.mk/bankarska_supervizija_i_riehulativa-en2.nsp

The higher value of the first indicator indicates that the bank has a larger liquidity reserve. Loans / Deposits ratio shows the extent to which loans are financed by deposits, and large and small banks have similar average values of 83%, while medium-sized banks have an average value of 102%. In terms of both indicators, medium-sized banks are those with a higher level of liquidity risk. Medium banks in N. Macedonia especially rely on external/secondary sources of funding loan portfolio, as shown on table 2.

Regarding the capital adequacy and capital to assets ratio, each group of banks has a value that is twice higher than the minimum of 8% determined by the law, during the whole observed period. This indicates appropriate capital strength for every group of banks.

3. EXPECTED PERFORMANCE OF BANKING SECTOR

The collapse of the Lehman Brothers Bank in 2008 started a chain reaction characterized by panic on the markets and a lack of trust, which led to spreading of the financial crisis into the global economy. The governments supported the financial system by increasing deposit insurance ceilings, providing guarantees for bank liabilities, and recapitalising banks being bailed out or wound down. They implemented fiscal measures to reduce the fall-out of crisis on the rest of the economy. This resulted in a mix of 'automatic stabilisers' (decreasing tax receipts coupled with increased government welfare payments as the economy slowed down) and targeted discretionary fiscal measures, such as additional public investment, tax relief and subsidies for part-time employment. These actions led to dramatic escalation of public debt and the creation of European sovereign debt crisis in 2008, which had its peak between 2010 and 2012.

COVID 19 has globally disrupted all the economic flows and all these adverse events are happening promptly and simultaneously in every national economy. It requires fast and efficient response considering support for non-financial subjects. The policy makers undertook measures, which indirectly

facilitated the financial burden of credit borrowers, households and legal entities. By understanding the importance of functioning of the real sector, in terms of servicing its financial obligations towards banks, the National Bank took effective response regarding the credit risk. The National Bank undertook measures that have direct influence on the most significant factors of bank's performance during economic downturns, the share of non-performing loans and reduced credit activity. Non-performing loans as one of the most vulnerable categories in the bank balance sheet have direct impact on banks' liquidity and solvency.

On the other side banks are deducting one source of liquidity supply till September 2020 and have greater exposure of risk tied to lowering the market value of assets. The National Bank justifies this measure by relying on the solid liquidity position of banking sector that comes from the stable deposit base. In addition, the National Bank through the monetary instrument – open market operations released in total amount of 15 billion denars, which is expected to provide further support to banks' credit activity, which in turn expects to have greater impact on their performance.

However, banking sector and the National Bank should preserve the confidence of depositors, because any kind of instability can cause deposit withdrawal, and this was one the main pillars of the banking sector stability during the Global Financial Crisis.

The performance of the banking system will be under great influence of COVID 19, because of the decrease in operating revenues, especially due to decrease in net – interest income and decrease not only in the credit demand, but in the overall demand for financial services. In addition, despite the postponement of the banks' obligation for recognizing the loan loss provisions, not later than 31.12.2020, this impairment has to happen due to the reduced creditworthiness of corporate clients and households. This will result in low, and even negative growth rate of profitability in the banking sector in 2020 with high degree of probability that it will continue by 2022, according to the latest macroeconomic projections by the NBRNM. It is still uncertain to determine the intensity and duration of adverse effects on banks, but if the mass extension for loan repayments is to be continued, the liquidity risk will be increased. Banks would be left out with less available funds for supporting the growth of credit activity (despite the effort of decreasing the base interest rate) and will have an immediate impact on banks' profitability and through that on banks' solvency.

4. CONCLUSION

As a result of the unfavorable macroeconomic conditions, banking performance will be disrupted. The stagnation in the economic flows will change the business behavior of economic entities, their financial position and revenue-generating capacity, by reducing their creditworthiness. This trend will be reflected in household sector. The increased credit risk, despite being postponed, will have an implication on the banks' bottom line performance at the end of this year. Depending on the efficiency with which the banks will manage the funds and the way they finance them, the performance of the banks will be with positive or negative growth.

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