

State of Play on the Sector Inquiry by the Office for Competition on bank loan interest rates for Small and Medium Sized Enterprises, interchange fees and merchant service charges

16 April 2014

Office for Competition

Introduction

1. The purpose of the Malta Competition and Consumer Affairs Authority (henceforth 'MCCAA') is the "attainment and maintenance of well-functioning markets for the benefit of consumers and economic operators"¹. To this end, one of the functions of the MCCAA is to promote and enhance competition². This function is carried out through the Office for Competition which is vested by law with the responsibility to apply and enforce the Competition Act. The Office for Competition also applies Articles 101 and 102 of the Treaty on the Functioning of the European Union in those cases where there is an effect on trade.
2. The Office for Competition has the responsibility to make markets work well for consumers and businesses. The Office believes that well-functioning markets are in the interest of businesses as well as consumers and that effective competition benefits the overall economy.
3. The mission of the Office for Competition is to promote effective competition in all sectors of the economy. Through the application of the competition rules, the Office has the responsibility to investigate and curtail anticompetitive practices and to study markets and recommend action so as to make markets more competitive.

¹ Article 4(1) of the Malta Competition and Consumer Affairs Authority Act (henceforth 'MCCAA Act') Chapter 510 of the laws of Malta.

² Article 4(2)(a) of the MCCAA Act.

4. The Office for Competition has in previous reports studied and provided recommendations to improve competition in other markets³.

5. In terms of Article 11A (1) of the Competition Act, where the trend of trade, the rigidity of prices or other circumstances suggest that competition may be restricted or distorted within the Maltese market, the Director General of the Office for Competition may conduct an inquiry into a particular sector of the economy or into particular type of agreements across various sectors. In the course of that inquiry, the Director General may request the undertakings or association of undertakings concerned to supply the information necessary for the application of Articles 5 and 9 of the Competition Act and Articles 101 and 102 of the Treaty on the Functioning of the European Union and may carry out any inspections necessary for that purpose.

6. Over the past months, there has been an intense debate regarding allegations of excessive charges and high interest rates on loans by the banks. In the light of this, the Director General of the Office for Competition has decided to take a closer look at the market and to open a sector inquiry in terms of Article 11A(1) to examine the prevailing competition conditions on the market, in particular with respect to interest rates on loans to SMEs, interchange fees and merchant service charges.

7. In the interest of transparency, the Director General of the Office for Competition is releasing this state of play document on its sector inquiry.

³School uniforms report – Preliminary and Final Reports available at: <http://mccaa.org.mt/en/consultations-publications>.

Objectives of the banking sector inquiry

8. The Office considers the objectives of the sector inquiry to be the following:
 - To study the market, in particular interest rates on SME bank loans, interchange fees and merchant service charges;
 - To identify competition concerns relating thereto, if any; and
 - To address those competition concerns.

9. The Office considers that it is important to ensure that the sector inquiry is appropriately focused in order to secure the effectiveness of the progress and outcome of the inquiry. The Office shall concentrate on the following factors which could have a substantial effect on businesses, particularly SMEs:
 - the extent of competition on the market;
 - the possibility for businesses to switch from one bank to another; and
 - transparency of the market and the possibility for customers to take an informed decision when selecting their preferred bank.

10. Competition on the market is affected by many factors such as barriers to entry and exit, productivity growth and demand. Competition tends to be more effective the less concentrated the market and the lower the entry barriers. Competition thrives when businesses and consumers are well informed on market opportunities and are able to choose between different products and services on the market.

The scope of the banking sector inquiry

11. The inquiry will focus mainly on interest rates on loans to SMEs, interchange fees and merchant service charges. The Office has decided to focus on business loans as these are core lending products essential for investment and expansion by businesses, especially for SMEs, which may find it difficult to obtain capital in any other way. In turn, investment and expansion have a direct impact on the growth of the entire economy. The inquiry will also cover in particular the domestic interchange fees charged by banks and the extent to which these influence the level of fees charged to merchants. The Office has decided to focus on the latter, as well as merchant service charges in general, since these may have a direct impact on final prices to consumers.

12. Competition in the banking sector in Malta has been the subject of a wide debate particularly over the last few months. In the last Budget Speech, the Minister of Finance expressed the Government's concern on the alleged high interest rates at which SMEs are borrowing and on high charges, noting that high interest rates and charges increase costs for businesses and erode the country's competitiveness⁴. It has been reported that banks' margins on loans are wider in Malta when compared to other EU member States and that in terms of SME interest rates there is room for further alignment with our peers⁵. A recent European Commission report has noted converging interest margins and has observed that higher interest rates on loans could reflect lack of competitive pressure⁶.

13. In the first phase of this inquiry the Office has been in contact mainly with the core domestic banks, the Central Bank and the Malta Financial Services

⁴ Budget Speech 2014 Ministry For Finance, Hon. Edward Scicluna, Page 36

⁵ Presentation on *Access to bank funding for businesses*, Professor Josef Bonnici, Governor of the Central Bank of Malta, January 2014.

⁶ European Commission, *Macroeconomic Imbalances Malta 2014*, page 25.

Authority and requested from them both quantitative and qualitative data. The Office has also held meetings with the General Retailers and Traders Union (GRTU) which represents SMEs in Malta, and the Chamber of Commerce. The findings of the Office will be based on the input submitted by a number of market players and stakeholders in the banking sector.

Potential outcomes of the sector inquiry

14. Market studies can lead to a range of outcomes. In the first place, it may result that no competition concerns actually exist and that the allegations made are not substantiated by the information gathered in the inquiry. On the other hand, the inquiry may confirm that the market is not working well. In the latter case, there are several options the Director General of the Office for Competition may consider in order to provide a remedy and restore competition on the market. These may include one or more of the following:

- recommend action where necessary - this is done as part of the Office's work to promote the development of and suggest measures to achieve healthy competition in the banking sector for the benefit of the Maltese economy;
- initiate an investigation where a breach of the EU and/or national competition rules is suspected; and
- accept commitments from the undertakings concerned to address the competition concerns found by the Director General.

Next steps

15. The Office for Competition is currently assessing the information that it has gathered so far. At this stage, it is still, however, in the process of gathering complete information. In the next few weeks, the Office plans to hold further meetings principally with the banks. In this preliminary phase, the Office is interested in the views of concerned third parties which it may not approach directly. The Office is also eager to hear the views of SMEs as it progresses on this sector inquiry. The Office invites those interested to submit their views, feedback and evidence in relation to this inquiry on the following postal or e-mail address.

By post:

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Comments should reach the Office for Competition by not later than 16th May 2014.

Following this preliminary phase, the Director General of the Office for Competition may in terms of Article 11A (4) publish a preliminary report on the results of the inquiry and again invite comments from interested parties.

Disclaimer

This document is without prejudice to the findings of the Office for Competition. Currently the analysis is not complete, data is still being gathered and the Office has reached no definite view on what course of action to take. The Office for Competition will decide on the way forward once the study is complete.