Why is the Macedonian Stock Exchange Unsuccessful?

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The Macedonian Stock Exchange (MSE) is not operating successfully. True, some of the parameters which we use to measure the success of a stock exchange have lately improved in the MSE. For instance, the monthly money volume has increased together with the number of transactions. But this is a far cry from success.

Who is to blame? Is the current management of the MSE incompetent?

I do not think so. Actually, I think the MSE has an excellent management team, doing their best to incorporate new trading techniques and to list new firms. The problems lie elsewhere.

A stock exchange is a very important financial market. It is a highly efficient and visible instrument of financing. In the West, it is used to finance most of the needs of corporations, way above financing available from banks. Individuals and firms save some of their income and invest it. The stock exchange is meeting grounds for savers wishing to invest their savings - and firms looking for investments.

Another function of stock exchanges is to assist governments in financing their internal borrowing requirements. Governments sell obligations (called bonds) to investors through the stock exchanges in their countries. A stock exchange is, therefore, an indispensable tool for re-financing national debt.

But a few conditions must prevail before a stock exchange functions properly.

The most important condition is the existence of a healthy, growing economy in the stock exchange's country. Investors flock to robust economies and shy away from sickly ones.

On the face of it, the Macedonian economy belongs to the latter category. High unemployment, low savings, retarded growth, a gaping trade and payments deficits. But this is an optical illusion. The economy is in much better conditions that most Macedonians would care to admit. The unemployment figures are skewed. They reflect efforts to evade paying social taxes - not real unemployment. The economy is growing, even by official estimates. The black economy is growing even faster. The deficits are covered by enormous capital infusions from donor countries. Macedonia is receiving more international credits per capita than Russia. It is always convenient to blame the worsening economic climate - but the cold, objective figures do not bear this out.

When an economy is growing - the profits of companies (including those listed in the MSE) will grow with it. This makes the shares of these companies an interesting buy.

Since no one is buying - we must look for the problem elsewhere.

A prospering stock exchange is linked to the existence of the right micro and macro economic management. Macedonia has more than its share of problems in this respect.

The process of transformation of businesses with social capital had four basic flaws:

first, it introduced no new management, ideas or capital to the beleaguered firms which were "transformed". The market simply does not believe that they were transformed. The same people run the same shows under a different hat.

Second, such transformation violates the concept of Hierarchy, a chain of command.

It blurs the distinction between labour (workers) and capital (owners). What is wrong with that is that a ship must have a captain - and only one. Someone must have the authority and the responsibility. Collective management is no management at all.

Moreover, innovation change and revitalization are all prevented. What change could come from the same set of worn out managers? How can thousands of owners decide to worsen the conditions of the workforce - if owners and labourers are one and the same? So, management is polluted by irrelevant, non-economic considerations: power struggles amongst groups of workers, social considerations and political ones.

We identified one villain. The other one is high (real) interest rates. When interest rates are high, three effects prevent the resuscitation of the stock exchange:

First, firms have high financing expenses (interest payments) - which reduces their profits. Second, it is not worthwhile to borrow money and to invest in shares.

Third, it is more tempting to invest money in bank deposits, yielding high interest rates - than in shares. High interest rates are the poison of stock exchanges.

The same is true for low savings rates. If people and firms do not save - there is no capital available for investment in stocks.

This, exactly, is the current situation in Macedonia : impossibly high interest rates coupled with exceedingly low savings. There is basic mistrust between clients and their banks. They prefer other ways of keeping their money.

But all the above is far from exhausting the list of pre-conditions for the proper functioning of a stock exchange.

Investors must have timely, accurate and full information about the firms that they invest in. This will allow them to respond in real time to developments in the company and to prevent losses. This will also make it difficult to cheat them - which is were we come to the question of accounting standards. Only lately have the accounting rules in Macedonia been revised to conform to the Western systems of accounting. Even now, the similarity is very slight. Macedonian firms maintain a double accounting system. One set of books is tax-driven. It is intended to show losses or profits at the whim of the management. An elaborate scheme of hidden reserves lies at the heart of the typical financial statements of the Macedonian firm. Another set of books - if they are kept at all - reflects reality. This is an enormous barrier to foreign investment - and foreign investors are the driving force in every modern stock exchange.

The trust of investors in the stock exchange is based on legislation to protect their property rights against the firm's management' against the authorities and against other investors who might wish to rig the market or manipulate the prices of stocks.

But legislation without an effective judicial and law enforcement systems is like a stock exchange without money. To enforce property rights in Macedonia takes ages and even then the outcome is not certain. Laws, regulations are in their embryonic stage and some of them seem to have had an abortion: they were hastily and unwisely copied verbatim from legal codices of other countries (Germany, Britain).

Last - but definitely not least - is the existence of a fair, transparent and non-corrupt marketplace. The stock exchange, the banks, the regulatory authorities, the police and the courts have to be above suspicion. For the market to be utterly efficient - it must be utterly free of any ulterior considerations and motives. Corruption distorts the market's allocative mechanisms and powers. It is easily discernible in dealings in the stock exchange for all to see. A stock exchange is, after all, the showcase of the local economy.

But there is a problem which towers above all other problems and it is almost endemic to Macedonia. It helps to explain much of the predicament of the stock exchange in Skopje. It is the fact that the market is missing its most important player: the Government.

Investors - both foreign and domestic - look for the Government to be active in the local stock exchange. Governments throughout the world use their stock exchanges to sell shares of state-owned enterprises to their populace. The stock exchange becomes a mechanism for the distribution of the national wealth - as embodied by the state owned enterprises - to all the citizens. As we said before, governments also use the stock exchange to borrow money from their citizens.

The Government of Macedonia does neither. It totally ignores the MSE. Not one company was privatized through the MSE. Not one Denar was borrowed from a Macedonian citizen through it. A government's activity in the stock exchange is proof that the government believes in it. Therefore, if it does not operate in the stock exchange - it proves that it does not believe in it. If the government does not believe in the stock exchange in its own country - why should the investors believe in it?

There are a few additional structural characteristics which are considered to be the hallmarks of a healthy stock exchange. But those are the by-products of all the above mentioned conditions.

A stock exchange must be liquid so that investors would be able to convert their shares into cash easily and expediently. It must include many investment options - professionally put, it must be diversified. This will allow the investors to choose from a variety of investments and also to reduce their risks by dividing their money among a few types of investments.

The management of the stock exchange can help it by introducing efficient trading techniques, computerized trading and settlement systems and so on. The faster investors meet their money when they sell their shares - the more they will be inclined to operate in the stock exchange that allows them that. The easier it is for them to liquidate their assets by meeting buyers - the more they will prefer to work in that stock exchange.

Investing in the stock exchanges in the markets of the emerging economies has been an unfortunate decision in the last three years. Stock exchanges from Russia to Hungary and from Lithuania to Poland have jeered wildly since the end of 1993.

They resembled a roller coaster in their performance, going up and down by tens of percents annually. There are exceptions to this rule. The Ljubljana Stock exchange, for instance. The trading volume there has gone up 10 times since December 1993 - and the market capitalization is up 30 times. But this is because of the performance of the general economy in Slovenia. In Croatia, the government is privatizing its holdings in state owned companies by auctioning shares to the public through the Zagreb Stock Exchange. This has helped it a lot.

Newly-established stock exchanges are highly volatile and very dangerous. Volatility goes hand in hand with risk. They are long term investments. Since 1988, they outperformed the more established stock exchanges in the world, like Wall Street.

But these stock exchanges are growing fast, they are cheap by any measure and they are the best investment that a country can make in its own future.

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European Stock Exchange Listings
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An axiom: When buying exceeds selling, the share price goes up. When selling exceeds buying, the share price goes down. The reasons for the buying or selling are secondary to the act of buying or selling.

The goal of your stock support plan is to encourage buying and discourage selling. One tactic in your battle for a strong share price is to list your company's shares on a European Stock Exchange.

Europeans are investors, not speculators. They'll carefully review the fundamentals of your company. I advise clients to sell their product or service in Europe. It gives your company credibility with potential European investors. As a rule, Europeans are more interested in the steak than the sizzle.

Does your company trade on the New York Stock Exchange (NYSE)? You should list it on the International (London) Stock Exchange. Does your company trade on the Over-the-Counter Bulletin Board (OTCBB)? You should carefully select one of Europe's risk-capital Stock Exchanges. Here are ten issues you should consider in selecting your European Stock Exchange.

1. Can you file in English?
2. Will the Exchange accept your SEC filings?
3. Where are the small capital investors? American companies consistently miss a primary source of small capital investors allied to each European Stock Exchange.
4. What will an Investor Relations program cost?
5. As your company grows, can you use your European OTC listing to list your shares on a stronger European or American Stock Exchange?
6. How do you arrange a European listing? The financial culture of each European Stock Exchange is different. There's an approved road to list your company. You must know it to succeed.
7. What does it cost to list? How does that cost compare to listing on Nasdaq or complying with SEC filing requirements?
8. Who can you trust?
9. How much of your stock will trade annually on this Stock Exchange?
10. How long will it take for your company to start trading?

Nasdaq is moving to consolidate U. S. Stock Exchanges, excepting the NYSE. The German (Frankfurt) Stock Exchange has a similar plan for Europe. Eventually, these two acquisition programs will merge. Currently it's faster, cheaper and easier to list an American OTCBB company in Europe than on Nasdaq. As European Stock Exchange consolidation progresses, this may no longer be true. If your shares trade in the States, you should think Europe in 1999.

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