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MARKET STRUCTURE AND COMPETITION IN THE SOUTH AFRICAN BANKING SECTOR**Abstract:**

This paper examines the relationship between bank structure, performance and competition in the South African banking industry. South Africa has a very concentrated banking industry with a C4 concentration ratio of over 80%. The structure conduct performance hypothesis would suggest that competition in the sector would therefore be very low. We apply the Panzar-Rosse approach to bank level data for the period 1997 to 2014 to assess the competitive environment in the South African banking industry. We estimate a revenue equation to obtain the H statistic. Changes in competition over the sample period are explored by estimating a time varying Panzar-Rosse H statistic. This also allows us to assume a gradual change in bank competition rather than a static equilibrium. We find that competition has increased over time. This result is consistent no matter how the time variable enters the revenue equation. The estimated H statistic suggests that banks operate in a monopolistically competitive market structure. Bank specific factors are generally consistent across alternative measures and in line with expectations. We also find that the increased concentration arising from the currency crisis in 2001/02 does not reduce the level of competition. This result is somewhat puzzling because the industry exhibits relatively high transactions fees in the larger banks.

Keywords:

bank performance, competition, Panzar-Rosse, South Africa

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