Establishing a Digital Participation Bank in North Macedonia: Opportunities and Challenges in Interest-Free Finance

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Abstract

This paper aims to explore the feasibility of establishing a digital participation bank in North Macedonia based on the principles of interest-free finance. This system has been part of ethical and equitable financial systems in the major Abrahamic religions. Thus, as interest-free finance becomes more popular worldwide, digital banking presents a new approach to incorporating these principles into the Macedonian banking system. Here, the purpose of the paper is to discuss the applicability of establishing a digital participation bank in North Macedonia based on interest-free finance principles, by drawing on global best practices. In that sense, this paper provides an analysis of the interest–free finance and intends to describe the banking environment in North Macedonia and the necessary regulatory and market changes. Furthermore, it offers recommendations for integrating ethical, interest-free finance into the Macedonian digital banking sector. Findings indicate that the country has strong potential, due to its diverse population, growing SMEs sector and demand for ethical financial services, but at the core, significant legal and institutional changes are required. Finally, the paper concludes with the opportunities that digital interest-free finance has in financial inclusion, investment attractiveness, and integration with the digital transformation strategy; while detected challenges refer to regulatory changes, consumer and institutional education.

Introduction

Interest-free finance, an ethical finance model that prohibits interest and is viable globally, originated from traditional systems and is historically practised in Abrahamic faiths. This model encourages risk sharing, real asset-based transactions, and social responsibility (Visser 2009; Saleem et al., 2013). Its success is evident in Türkiye, Bosnia and Herzegovina, and parts of Europe, where participation banks thrive in supportive regulatory environments, with Türkiye's government being a key driver (Derbel et al., 2011).

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The universality of the global success of digital banking in the interest-free finance sector is proven by its imitation all over the world. The UK has emerged as a leader in ethical finance, with Al Rayan Bank offering a range of interest-free products, including Sukuk Islamic bonds for infrastructure projects. These institutions have been able to cater to a diverse clientele, including non-Muslims, with regulatory support. The success of sukuk issuance shows that interest-free finance is compatible with the Western regulatory systems and thus could be a viable alternative for socially responsible investment (World Bank, 2017).

The market for interest-free finance has a niche audience in Germany, and this niche is focused on sustainability and ethical investing. Some financial institutions in Germany incorporated principles of responsible investing that are consistent with the principles of interest-free finance, which include the avoidance of exploitative industries. Although interest-free finance is still a small part of the market, it is appealing to ethically conscious consumers who are looking for transparent and sustainable financial products (Apaydın, 2021).

In South Africa, FNB Islamic banking shows that interest-free finance can easily be adopted in a multi-faith and secular environment. Furthermore, South Africa's regulatory framework has been very efficient in facilitating the growth of interest-free financial products, thus becoming an example of how to incorporate them into multicultural markets (Gündoğdu, 2018).

The Canadian model of interest-free finance shows that the model is flexible enough for secular and multicultural societies. Canadian financial institutions have focused on ethical investments and community-driven financing models as they expand their appeal to socially conscious consumers (Credit Union Central of Canada, 2012).

Additionally, the experience of Türkiye shows that using digital channels extends the coverage of interest-free financial services to more people and provides ethical finance to the unbanked (Abdul-Rahman, 2014). From this point of view, interest-free finance has great potential for North Macedonia and other Balkan economies when combined with digital banking (Abdul-Rahman, 2014; Visser, 2009). Therefore, this paper aims to explore the feasibility of establishing a digital participation bank in North Macedonia based on interest-free finance principles. The research methods include analysis of the current banking landscape, regulatory environment, and market readiness, with a focus on integrating digital banking and interest-free finance in North Macedonia. The discussion in this paper is focused on the distinction between religious motivations and universal ethical finance logic, emphasizing SME support, and sustainable banking innovation, while the content is structured around the applicability of interest-free finance in North Macedonia, the setting of the Macedonian banking sector, in terms of its legal framework and Fintech emergence, and finally elaborates on the establishment of digital participation bank and its socio-economic impact.

Applicability of Interest-Free Finance in North Macedonia

Globally, there is a rising awareness and demand for ethical and interest-free financial products that emphasise transparency, social responsibility, and sustainable development. Interest-free finance models, such as mudarabah (profit-sharing) and musharakah (joint venture), appeal not only to religiously observant consumers but also to ethically conscious individuals, SMEs, and investors. These models align with modern principles of stakeholder capitalism and inclusive finance. In that sense, according to Halal Times (2024), *"the surge in popularity of interest-free banking can be attributed to its ethical approach and the increasing awareness and demand for Shariah-compliant financial products, as a response to the needs of Muslims who want to manage their finances in a way that is consistent with their religious beliefs, as well as non-Muslims who seek ethical banking alternatives"*. Although Islamic finance has popularised these practices, their implementation in countries like the UK, Canada, and South Africa shows that religious affiliation is not a prerequisite for adoption. In these environments, regulatory innovation and ethical consumer behaviour have driven the demand. For the purpose of clarifying the conceptual distinction and overlap between Islamic and Interest-free finance, Table 1 summarises their key differences.

Table 1
Distinction between Islamic Finance and Interest-Free Finance

	Islamic Finance	Interest-Free Finance
Definition	Financial system based on Shariah Law, which is characterised by – prohibition of Riba, Gharar, and Maysir; avoidance of trade in unlawful goods	An alternative to an interest-based financial system that eliminates the interest, but does not necessarily follow Shariah Law

Continuation of Table 1

Distinction between Islamic Finance and Interest-Free Finance

	Islamic Finance	Interest-Free Finance
	and services; and follows the principles of justice and equity.	or religious principles.
Core principles	Profit and loss sharing, asset backing, ethical investments and religious compliance.	Economic ethics, transparency and social responsibility, secular in foundation
Scope	Banking, capital markets (eg, Sukuk), insurance (takaful), leasing, investments.	Banking, investment
Governance and Compliance	Oversight by Shariah Boards, responsible for overseeing activities and introducing financial products.	Governed by ethical codes, regulations, binding contracts or membership in alliances, such as the Global Alliance for Banking on Values. (No Shariah compliance needed.)
Products and instruments	Mudarabah; Musharakah; Bai' al-Salam (prepayment financing); Qard al-Hasan; ijarah; takaful etc.	Profit and loss sharing (Mudarabah, musharakah), prepayment financing, equity-based lending, community finance, microfinance, i.e. zero-interest loans or group lending for low-income borrowers
Users	Muslims, ethical investors	Ethically motivated users, socially conscious investors, and cooperatives
Examples of financial institutions	Al Rayan Bank, Islamic Development Bank, etc.	Triodos Bank, cooperative credit unions, and P2P lending platforms with zero-interest lending models

Source: Authors

In North Macedonia, the demand for interest-free finance products could be driven by: i) the consumers and businesses looking for ethical banking options, and ii) the attraction of foreign investors from countries where interest-free finance is prevalent. This depends mostly on North Macedonia's diverse population with a significant Muslim community, which might be more inclined towards interest-free financial products due to religious beliefs. Secondly, the country's economic landscape is characterised by a growing SME sector and increasing foreign investments, and contracts like *mudarabah* or *musharakah* can provide vital support to SMEs by encouraging entrepreneurship, the establishment of new companies and finally, contributing positively to economic growth and job creation.

Given the similarities that exist between Islamic and interest-free finance, the closest research done in the area of interest-free finance in North Macedonia is the research conducted by Abdullahi & Shaharuddin (2016), which investigated the potential for introducing Islamic banking services into North Macedonia's existing banking system. This research showed that 68.4% (out of 500 respondents in Tetovo-N. Macedonia) believed bank interest is unethical, reflecting a strong understanding of the prohibition of interest (Riba). Additionally, 92.8% of respondents indicated they would use Islamic banking services if available through an Islamic banking window, highlighting significant demand. Moreover, 74.4% agreed that nationwide Islamic banks would attract users, showing significant support for such services. These findings show that in North Macedonia, there exists a public interest in ethical banking finance models, firstly driven by the desire for greater transparency, accountability, and social responsibility in financial practices. These practices can be seen to align banking activities with broader societal values, enhancing trust in financial institutions and contributing to sustainable economic development (European Investment Bank, 2024). Additionally, the development of the Fintech sector can contribute towards the transformation of the banking industry, enabling conventional banks to integrate many ethical practices into their value chains.

Despite its appeal, interest-free finance remains underdeveloped in North Macedonia due to its conventional banking infrastructure. However, given the previous evidence, there is a potential for integrating interest-free finance, but the regulatory framework would need adjustments to accommodate Sharia-compliant financial products. This includes the establishment of regulations that allow for interest-free financial products, such as profit-sharing (*mudarabah*) and joint venture (*musharakah*) contracts. At the same time, interest-free transactions require specific taxation and accounting standards. For instance, regarding taxation, interest-free transactions should not be disadvantaged when compared to conventional ones, or, for example, in the case of *murabaha* contracts (where the same asset is sold and resold), to avoid double taxation. In profit and loss sharing arrangements (like *mudarabah*), the capital provided by the Rab-ul-Mal is recorded as an investment while crediting the cash item. Afterwards, profits are recognised when earned and distributed according to the agreed ratio, debiting the Cash, and crediting the Mudarabah profit (Mia, 2016). In a nutshell, the regulatory changes would require greater transparency of the terms and conditions of interest-free financial products to ensure that consumers understand the profit-sharing and risk-sharing mechanisms and modification of consumer protection laws that address the specific risks related to them.

Current Banking Landscape in North Macedonia

The banking system of the country is still quite traditional and does not include many practices of interest-free finance. In its process of modernisation of the economy and integration into the European Union, the country could use a digital participation bank that would expand the range of services and attract customers who are concerned with the ethical aspects of the company's activity (Derbel et al., 2011). The experience of Bosnia in the use of interest-free finance can be followed, and the practice of Türkiye in the use of participation banks and their development, including the use of technology. Such an initiative can help North Macedonia to align with the global standards of ethical financial practices and can also contribute to the overall economic and social development.

North Macedonia's financial system is bank-based, characterised by banks' significant role in financial intermediation and economic activities. Banks are the primary financial intermediaries, holding about 80.4% of the total assets in the financial system (NBRNM, 2024). Moreover, given the stage of financial development that corresponds with economic development, it means that Macedonian banks are primarily focused on commercial banking activities, i.e., they follow a traditional banking model. The predominant source of funding for banks is deposits, derived from the domestic private sector and accounting for approximately 80% of their liabilities, highlighting the substantial confidence that the Macedonian population places in these financial institutions. (NBRNM, 2024). Additionally, their loan portfolio is almost evenly split between households and corporate loans, giving a small preference for households since it enables lower credit risk and better portfolio diversification (EBA, 2021).

While traditional banking practices dominate, there is a growing shift towards digital transformation. Banks are increasingly adopting digital technologies to enhance their service delivery and operational efficiency and better meet customer needs. According to findings by Stanoevska et al. (2023), digitalisation is a major challenge for the Macedonian banking system, driven by new payment regulations and competition from fintech providers. Banks often view fintech as a cost rather than a benefit, or as a complementary partnership that can give advancement in their operations. Banks need to adopt new technologies and manage associated risks to financial resilience, inclusion, and consumer privacy. Empirical evidence shows that Macedonian banks are digitising in several areas, such as digital identity services, digital payment methods, online account management, mobile banking applications, and online lending applications. This emphasises the need for traditional banks to innovate and invest in digital solutions when offering financial services, reinforcing the statement that the banking sector still lacks significant competition from fintech companies (Danevska, 2020). Fintech companies are companies that use technology in the areas of banking services, payments, data analysis, capital markets and financial management (Huang, 2015). National Bank's study of 2020 showed the absence of entirely new fintech business models, such as digital-only challenger banks or equity-based crowdfunding platforms. Even today, the fintech environment does not recognise these kinds of digital banks or crowdfunding platforms in North Macedonia. What can be noticed in the current financial industry, in terms of non-bank financial companies, is the operation of fintech companies in the areas of risk assessment, credit scoring, lending, and investing (Table 2).

Table 2
Examples of non-bank financial companies in North Macedonia that use advanced technology

Examples of non-bank financial companies utilising advanced technologies	**Advanced technology and application**
Tigo Finance Macedonia	Uses advanced algorithms for quick loan approvals and risk assessment.
Iute Credit	Implements digital platforms for loan applications and customer service, making the process more efficient.
Credissimo	Using AI and machine learning to streamline loan processing and improve customer experience.
Mogo Finance Macedonia	Utilises technology for vehicle financing, including online applications and automated credit scoring.
Factor Trust	Employs big data analytics to provide alternative credit data and improve credit reporting
Blockchain EcoToken	Leverages blockchain technology for secure and transparent crowdfunding

Source: Authors' research

This is largely due to the delayed adoption of an evolving regulatory framework, where significant steps and actions should be taken to support the growth and integration of fintech companies in North Macedonia, which will support innovation and growth in the financial sector. Currently, fintech companies are subject to the same regulations as traditional financial services, with no special regime specifically for fintech. However, the Payment Services and Payment Systems Act, effective from January 2023, aligns with EU directives and aims to modernise the payment services industry, facilitating the entry of new fintech providers. Additionally, the National Bank of the Republic of North Macedonia has developed a Fintech Strategy for 2023-2027, focusing on technological innovation, regulatory alignment, and financial inclusion. Additionally, the country is considering a regulatory sandbox model to support fintech innovation, particularly in cryptocurrencies. Recent reforms in regulatory frameworks, including the amendments to the Company Law, also aim to simplify business operations and enhance the competitiveness of the fintech sector. This is expected to further push the development of the fintech sector and, more importantly, to significantly influence the business models of traditional banks (Danevska, 2021).

On the other hand, Fintech companies can strengthen ethical banking practices, such as interest-free financial products, by promoting financial models that emphasise positive societal impact. By analysing real-world examples (such as those of Challenger Bank Triodos UK), it can be noted that fintech companies demonstrate considerable maturity and expertise in leveraging their innovations to adhere to ethical principles (Danevska, 2024). Furthermore, these examples can also be used as guidance for traditional banks in the manner of forming mutually beneficial relationships, particularly in impact investment, raising awareness of ethical financial practices, promoting sustainable behaviour among all stakeholders, and even interest-free financing.

Establishing a Digital Bank with Interest-Free Finance in North Macedonia

The establishment of a fully digital bank with interest-free products in North Macedonia first requires implementing many changes in the regulatory environment. This involves collaboration between the government, regulatory bodies, financial institutions, and the community to ensure a smooth transition and successful adoption of digital and interest-free finance.

In the case of the establishment of a digital bank, North Macedonia can follow the case of the United Kingdom, as a leader in the global digital banking industry. Many of the UK's digital banks initially started as fintech companies, primarily offering payment services, and over time, as they grew and demonstrated their capabilities, they applied for and were granted full banking licenses (Mbama and Ezepue 2018). For example, Monzo and Revolut began as Fintech startups granted e-money licenses, enabling them to provide payment solutions, prepaid cards, and currency exchanges. Later, they expanded their services and obtained banking licenses to offer a broader range of financial products. This approach allowed them to build a customer base and refine their technology before taking on the full regulatory responsibilities of a bank.

According to the new Law on Payments and Payment Systems (90/2022 and the Amendments from 64/2024), which was aligned with the newest EU PSD2 directives, e-money institutions can provide services in the area of payments, issuing e-money, managing payment systems, and currency exchange. The funds received by payment institutions and e-money institutions from payment service users do not constitute deposits or other repayable funds (Article 15, paragraph 2). Additionally, according to the same article, point 4, the issuer of electronic money is not allowed to calculate or pay interest or offer any other benefit during the period in which the holder of the electronic money retains the electronic money. Regarding the issuance of credits, according to the Article 12: "A payment institution or an electronic money institution may approve a credit line related to the payment services if: i) The credit line is auxiliary and approved solely to execute payment transactions; ii) The credit granted for providing payment services in the territory of a third country is repaid within a period not exceeding 12 months; and most importantly iii) the credit line *is not approved from the funds received or held for executing payment transactions*, nor from *the funds received in exchange for issued electronic money that are held* by Article 32 of this law; and when concluding and implementing the credit line agreement, the provisions of the Consumer Protection Law regarding consumer credit agreements are appropriately applied."

So, in terms of regulatory requirements for being bank-chartered, the transitioning of Macedonian fintech from an e-money license to a full banking license would involve several challenges and restructuring of the company that includes: an increase in initial capital (from 7.800.000,00 denars to 310.000.000,00 denars), preparation of detailed business plans, risk management frameworks that follow internal acts and decisions of the National Bank, related to credit, market and operational risk, acquiring licenses and approval for bank's key personnel, upgrades to IT systems and operational infrastructure for a broader range of financial banking services (including collecting deposit and lending) and finally participation in the Fund for deposit insurance, ensuring that retail and sole proprietors 'deposits are protected up to a certain amount. Furthermore, a bank in North Macedonia can be established as a joint stock company, while for comparison in the UK, Monzo is a private limited company.

On the other hand, the introduction of interest-free financing in North Macedonia, currently cannot occur under the Law on Banks, whereby Article 2, point 23 states "Credit is the provision of a certain amount of money in exchange for the repayment of the approved and outstanding amount, together with interest or together with interest and fees calculated on that amount." However, according to the Law on Financial institutions article 3, point 3, *"credit is the provision of a certain amount of money in exchange for the repayment of the approved and outstanding amount, together with the interest and/or fees calculated on that amount."* This definition is closer in practice to what a Sharia-compliant bank – for example, Al-Rayan Bank UK charges for financing a residential investment in the form of rent payments or profit charges (referring to the agreement Ijarah, i.e., leasing). This type of mortgage is used both for financing a house purchase and for existing homeowners switching from an interest-bearing mortgage. (HM Land Registry, 2023). Additionally, in the case of interest-free financing, Monzo offers and buy now, pay later (BNPL) service that allows customers to extend the cost of purchases over three months with no interest, for purchases between £30 and £3,000.

These examples illustrate that the UK provides a supportive environment for both digital banks and interest-free financial products. This is based on a robust regulatory framework that ensures that interest-free financial products are accessible. These laws also align with EU directives that accommodate both bank and non-bank financial institutions offering Sharia-compliant financial products, conventional and alternative interest-free finance models.

Therefore, from legal aspect, the establishment of a digital interest-free bank in North Macedonia would require amendments in the Law on Banks (by taking into consideration the means of repayment and the operation of a digital-only bank), or this entity might be established as non-bank financial institution where its products and services would comply with an upfront defined values framework, or guiding principles, or certified by a Shariah board or committee (Emirates Institute of Finance, 2025).

Potential Economic and Social Impacts

Interest-free finance has the capacity to change the world by promoting financial inclusion, ethical banking, and the development of small and medium enterprises. In this regard, a digital participation bank based on interest-free finance could be a solution for SMEs in North Macedonia to get alternative financing that will help them to grow and create new products and services while observing the ethical principles in business. Some examples of interest-free financing products include mudarabah, which is profit sharing, and musharakah, which is a joint venture, as alternatives to traditional loans that come with interest rate payments and, therefore, do not make the client's business incur debt and grow. These arrangements guarantee that the financier and the business owner share both the risk and reward in the business, and this is done in a way that is more conducive to the risk taken in new and emerging enterprises (Ahmed, 2002).

The use of interest-free finance also increases financial inclusion, as the SMEs who may not be willing to get financing from conventional interest-bearing channels can be reached. In North Macedonia, where SMEs are important for growth and employment, interest-free finance can help break the barriers to credit for the smaller firms. Interest is, therefore, excluded from the transactions, which makes the participation banks to provide more affordable financing options that are consistent with the business owners 'ethical values, especially those who may not want to get financing from interest-bearing sources for cultural or religious reasons (Ali & Al-Owaihan, 2008).

In addition, the digital infrastructure of a participation bank can improve the availability of financial services in the unserved areas of North Macedonia, including SMEs and individuals who cannot easily access the conventional banking system. Interest-free financial services can be provided to a large extent through mobile and online platforms, and SMEs in rural and remote areas can also be able to access the necessary funds for business growth. This digital strategy promotes a more inclusive financial system in which entrepreneurs can embrace the principles of ethical finance. This integration with ethical finance will further enhance the competitive standing of the North Macedonian SMEs in the regional as well as international markets because consumers would be more conscious of buying from companies that are socially responsible and environmentally friendly (Ali & Al-Owaihan, 2008).

North Macedonia can also use the principles of interest-free finance to develop new and innovative funding models, such as crowdfunding, B2B, B2C, and C2C funding. These models also follow the principles of interest-free finance as they are based on direct investment in tangible projects and community-based funding. For example, profit-sharing arrangements in crowdfunding can increase public engagement by allowing backers to share in a venture's success, thus leading to beneficial relationships between investors and SMEs. This way, the capacities and capabilities of businesses are enhanced by providing them with a wider pool of ethical investors, often at lower costs than from traditional financing methods (Obaidullah, 2008; Ayub, 2007).

Conclusion

From the given case studies in various countries around the world, the regulatory overview and the current state of the financial environment in North Macedonia, the implementation of interest-free finance in North Macedonia is a viable but complicated proposition. The increasing global demand for ethical and/or Sharia-compliant financial services offers a great chance for such products in North Macedonia, especially given that it has a large Muslim population and a rapidly developing SME sector. Based on the overview of the current financial landscape in the Republic of North Macedonia, in terms of the existence of a conventional banking system, the emergence of Fintechs as a catalyst for the establishment of a digital interest free bank and the financial legal framework, the uptake of interest free finance models has its challenges. These challenges call for changes in the legal framework, enabling banks to engage in offering interest-free financing products. Additionally, this would require educating and training financial institutions and regulators' staff. Setting the ground for interest-free financial products enables not only ethical banking products, community financing, SMEs support, but and facilitation of entry of foreign investments that would diversify the offerings of financial products and boost the economic development.

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Ustanovitev digitalne participativne banke v Severni Makedoniji: priložnosti in izzivi brezobrestnega financiranja

Izvleček

Namen tega članka je raziskati izvedljivost ustanovitve digitalne participativne banke v Severni Makedoniji na podlagi načel brezobrestnega financiranja, sistema, ki je del etičnih in pravičnih finančnih sistemov v glavnih abrahamskih religijah. Ker brezobrestno financiranje postaja vse bolj priljubljeno po vsem svetu, digitalno bančništvo predstavlja nov pristop k vključevanju teh načel v makedonski bančni sistem. Namen tega članka je ob upoštevanju najboljših svetovnih praks razpravljati o izvedljivosti ustanovitve digitalne participativne banke v Severni Makedoniji na podlagi načel brezobrestnega financiranja. V tem smislu ta članek ponuja analizo brezobrestnega financiranja in opisuje bančno okolje v Severni Makedoniji ter potrebne regulativne in tržne spremembe. Poleg tega ponuja priporočila za vključitev etičnega, brezobrestnega financiranja v makedonski sektor digitalnega bančništva. Ugotovitve kažejo, da ima država velik potencial zaradi raznolike populacije, rastočega sektorja malih in srednje velikih podjetij in povpraševanja po etičnih finančnih storitvah. Vendar so v osnovi potrebne pomembne pravne in institucionalne spremembe. Članek navaja priložnosti, ki jih brezobrestno digitalno financiranje ponuja za finančno vključevanje, privlačnost za naložbe in integracijo s strategijo digitalne transformacije, medtem ko so ugotovljeni izzivi povezani z regulativnimi spremembami ter izobraževanjem potrošnikov in institucij.

Ključne besede: digitalno bančništvo, brezobrestno financiranje, etično financiranje, digitalna transformacija