

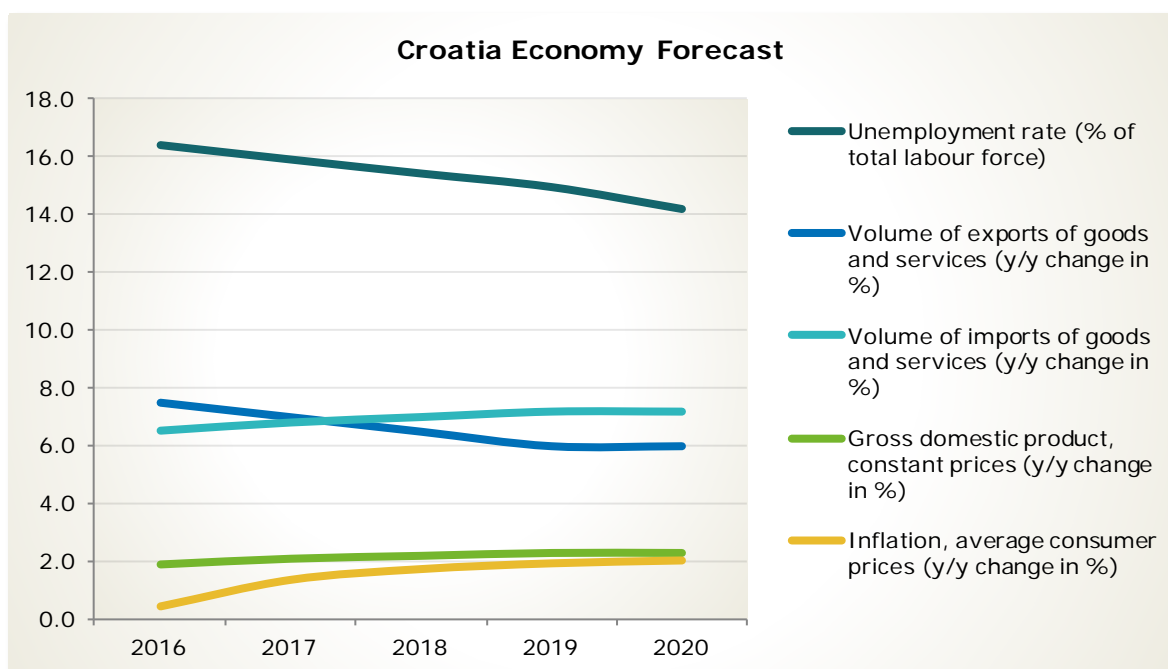
CROATIA ECONOMY REPORT Q1 2017

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1. MACROECONOMIC SNAPSHOT AND FORECAST

CROATIA – MACROECONOMIC SNAPSHOT AS OF Q1 2017	
GDP Growth	2.5% y/y
Industrial output	1.9% y/y
Industrial sales	9.2% y/y
Wholesales	4.4% y/y
Retail sales	7.1% y/y
Average annual deflation	0.5%
Unemployment rate	14.1%
Number of building permits	41.4% y/y
Money supply growth	3.7% y/y
Household loans	-0.9% y/y
CROBEX blue-chip index	8.2% q/q
Gross external debt	EUR 43.804 bln
Current account deficit	EUR 1.528 bln
Net FDI inflow	EUR 427 mln
Foreign trade deficit	EUR 1.838 bln
Number of foreign tourist overnights	-1.7% y/y

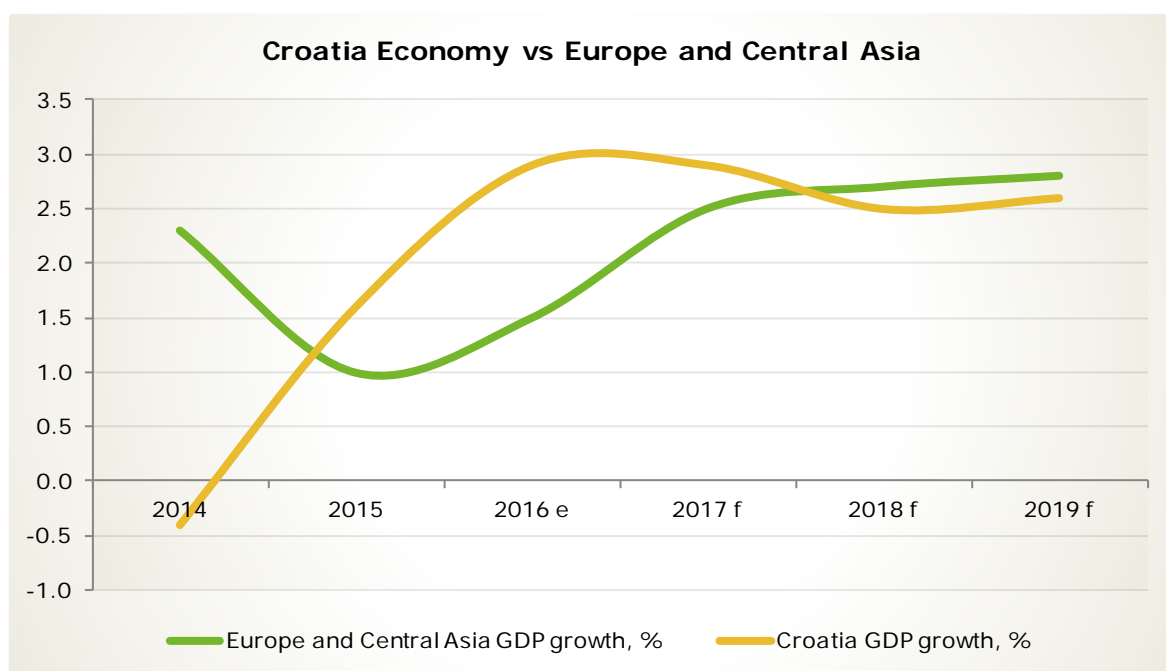


Source: International Monetary Fund (IMF) World Economic Outlook Database - April 2016

The International Monetary Fund (IMF) expects GDP growth in Croatia to accelerate to 2.9% in 2017, up from 2.5% in 2016 as reported by the country's statistical institute (DZS). In 2018 and 2019, IMF forecasts growth of 2.5% and 2.6%, respectively. The growth projections are based

on an anticipated solid export and tourism performance and a continued recovery in domestic demand. Private consumption is expected to be supported by recovering wages, better employment prospects, and decreasing the process of deleveraging. EU fund absorption and expected budget consolidation will increase public and private investments.

However, according to the IMF, the risks to the forecasts continue to be tilted to the downside. External demand could slow due to the economic uncertainties in the EU and global interest rate increases could lead to higher costs for the large public and private financing needs. Trade and tourism could be hurt by the refugee crisis and delay in reforms could bring fiscal risk through wage and social benefits increases, as well as slower absorption of EU structural and investment funds.



Source: World Bank, *Europe and Central Asia Economic Update*, May 2017

According to a recent World Bank (WB) forecast, the Croatian economy will grow by 2.9% in 2017, up from 2.5% in 2016, as reported by DZS. In 2018-2019 the GDP is projected to grow at around 2.6%, on strengthened personal consumption, tourism and EU funds absorption. The bank expects the current account surplus to decline to around 1.6% in 2017-2019, given a high import-reliance of the growth model.

New fiscal expansion and domestic policy uncertainty poses a risk to the WB forecasts. In addition, the still high levels of private and public sector indebtedness make the country vulnerable to the Fed's monetary tightening and to increasing the volatility on the financial markets.

Croatia – GDP, Inflation, Current Account Balance and FDI Dynamics (y/y change in %)

	2014	2015	2016 e	2017 f	2018 f	2019 f
Real GDP growth, at constant market prices, y/y change in %	-0.4	1.6	2.9	2.9	2.5	2.6
Private Consumption	-0.7	1.2	3.3	3.5	2.7	2.6
Government Consumption	-1.9	0.6	1.7	1.0	1.2	2.0
Gross Fixed Capital Investment	-3.6	1.6	4.6	6.0	7.0	6.5
Exports, Goods and Services	7.3	9.2	6.7	5.6	4.2	4.4
Imports, Goods and Services	4.3	8.6	7.3	7.0	6.4	5.9
Real GDP growth, at constant factor prices (by sectors)	-0.1	1.4	2.8	2.9	2.5	2.6
Agriculture	0.0	-0.4	0.1	2	2.1	2.2
Industry	0.5	1.9	4.3	2.8	2.7	2.7
Services	-0.3	1.3	2.4	3	2.4	2.6
Inflation (Consumer Price Index)	-0.2	-0.5	-1	1	1.5	2
Current Account Balance (% of GDP)	2.0	5.3	2.7	1.9	1.5	1.2
Net Foreign Direct Investment (% of GDP)	1.6	0.6	4.3	3.1	3.1	3.1

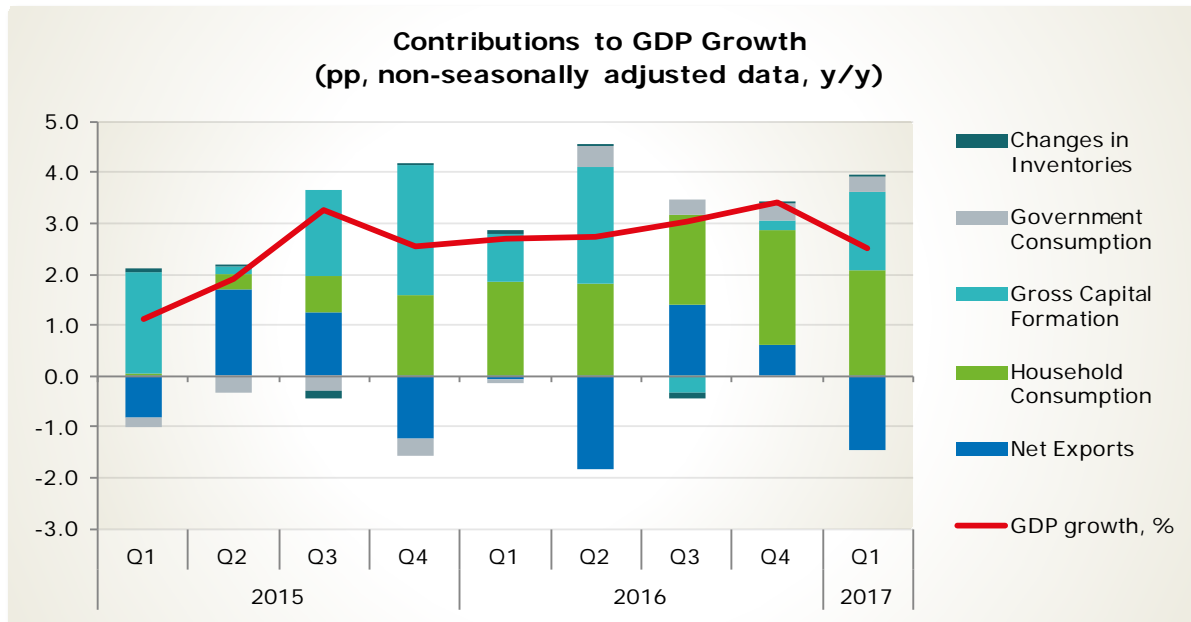
Source: World Bank, Europe and Central Asia Economic Update, May 2017

2. REAL SECTOR**2.1. GROSS DOMESTIC PRODUCT (GDP)****GDP went up by real 2.5% y/y in Q1 2017**

The country's GDP grew by a real 2.5% y/y and totalled HRK 76.947 bln in Q1 2017, according to preliminary data of the Croatian Bureau of Statistics (DZS). The main drivers behind the y/y economic growth were household consumption and capital investments.

Final consumption, which accounted for 81% of the GDP, expanded by 3.0% y/y and contributed by 2.4 pp to the GDP growth during the first quarter. Gross capital formation went up by 5.4% y/y, contributing with 1.5 pp to the GDP expansion. Imports grew faster than exports, by 10.1% and 8.6%, respectively and the trade gap widened to HRK 8.1 bln in Q1 2017 from HRK 7.0 bln in Q1 2016. As a result, the foreign trade took away 1.5 pp from the GDP growth.

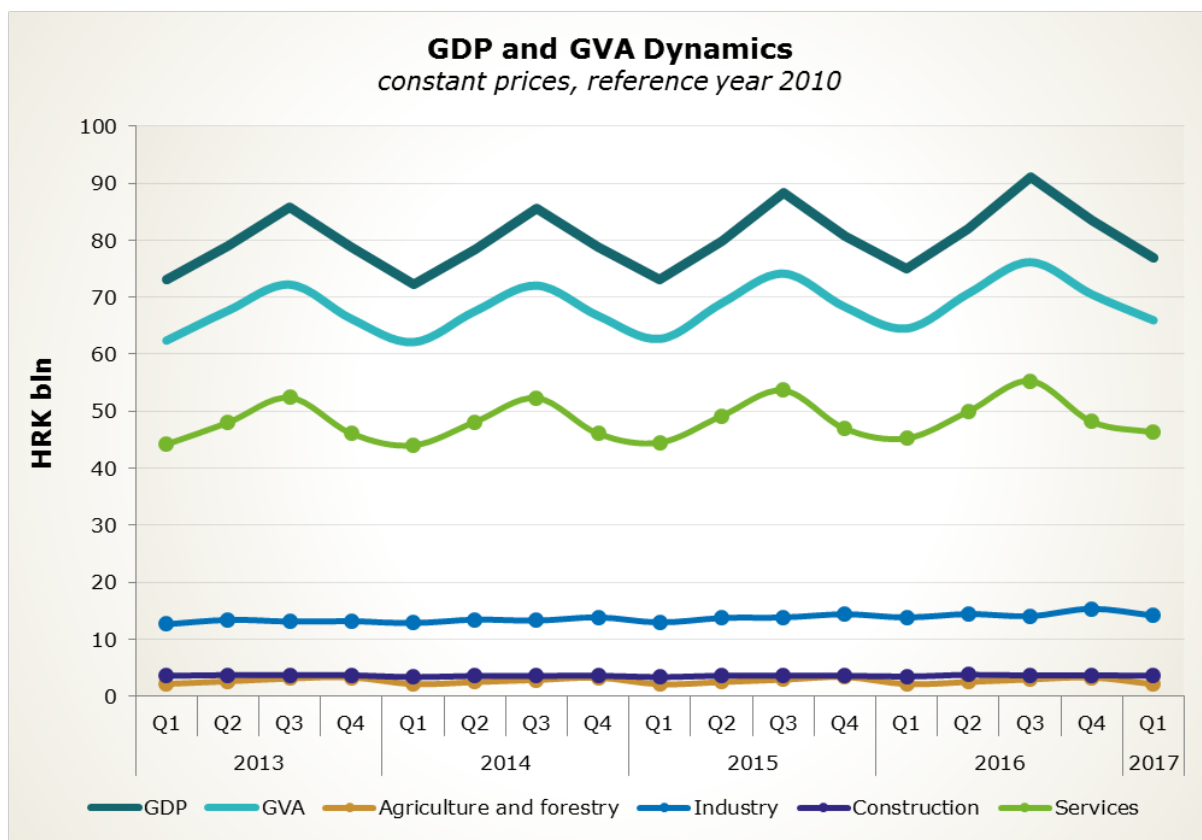
In the first three months of the year, the Croatian economy decelerated its pace of growth by 0.9 pp compared to the annual growth rate of 3.4% in Q1 2016. According to the Croatian National Bank (HNB), the lower rate of GDP growth is due to the Easter Holidays, which in 2016 fell in the first quarter and in 2017 in the second quarter and the smaller number of working days because 2016 was a leap year. As a result, consumption levels were lower in Q1 2017.



Source: DZS; SeeNews calculations

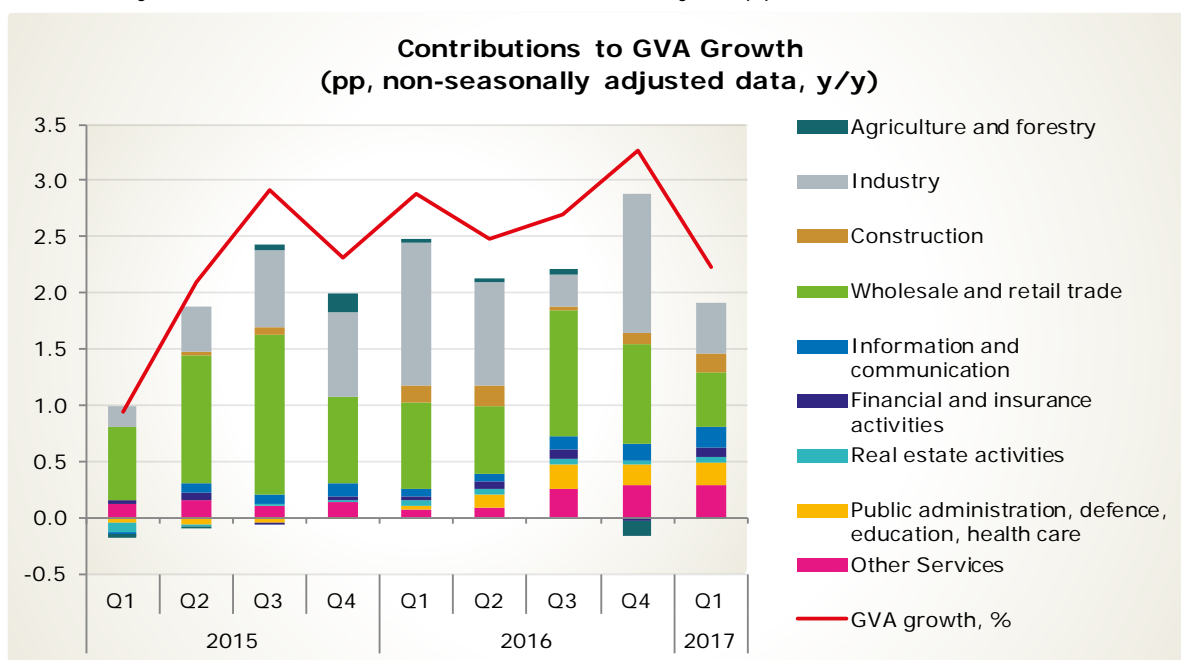
Note: Non-additive data due to direct chain-linking of GDP and its components. Contribution of changes in inventories has been derived as a residual.

The gross value added (GVA) generated by the national economy grew in value by 2.2% y/y in Q1 2017 and totalled HRK 65.957 bln. The industrial sector increased by 2.3% and its share in the GVA structure remained unchanged at 21%. The construction sector went up by 3.6% and its share in the GVA was 5.4%. The services sector recorded a 2.2% annual increase, slicing a 70.2% share in the GVA. The agricultural sector decreased by 0.4%, while its share in the GVA remained at 3.2%.



Source: DZS

Retail and wholesale trade was the largest contributor to GVA growth in Q1 2017, with 0.5 pp, followed by the industrial sector which contributed by 0.4 pp.



Source: DZS; SeeNews calculations

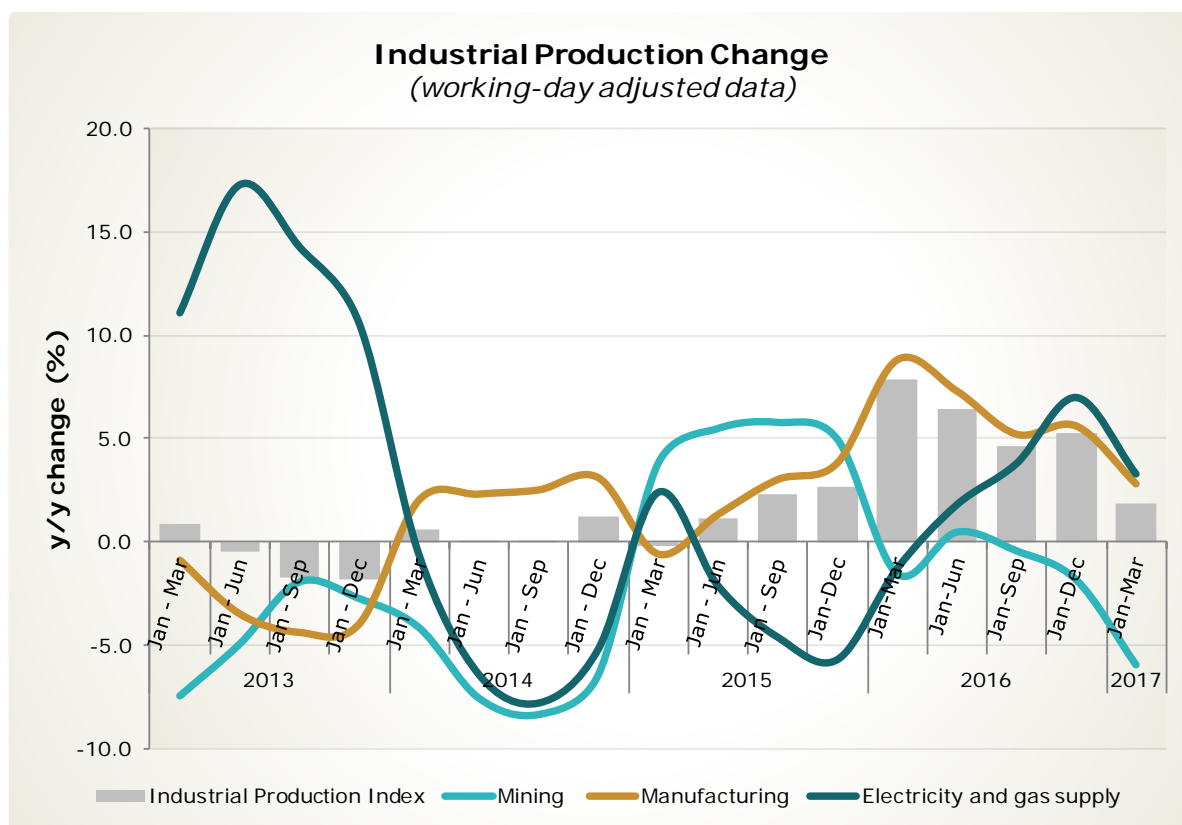
Note: Non-additive data due to direct chain-linking of GDP and its components.

2.2. INDUSTRIAL OUTPUT

Industrial output slowed pace of growth in January - March 2016 to 1.9% y/y on the bad weather

Industrial output went up by 1.9% on the year in January to March 2017, according to DZS data. This is significant slowdown compared to Q4 2016 when industrial production expanded by 5.3% y/y and is most probably due to the bad weather conditions in January and February 2017.

The growth during the quarter was backed by the 3.3% annual increase of the electricity and gas production and the 2.8% annual increase of the manufacturing sector. The production of the mining sector fell by 5.9% y/y.



Source: DZS

2.3. INDUSTRIAL SALES

Industrial sales surged by 9.2% y/y in January - March 2017 on energy price recovery

In contrast to the slowdown in the industrial production, industrial sales surged by 9.2% y/y in the first three months of 2017, compared to a 3.2% annual decrease in Q4 2016, according to

DZS. In March 2017 alone, industrial turnover on the domestic market increased by 8.0% y/y, while the non-domestic turnover jumped by 28.8% y/y.

The industrial sales were pushed up by the 112.5% annual jump of sales in the energy sector because of the oil price surge on the World markets. Capital goods sales went up by 17.3% y/y, while consumer durables grew by 8%.

2.4. WHOLESALE/RETAIL

Retail sales increased by 7.1% y/y, wholesales up 4.4% y/y in Q1 2017

Retail sales registered annual increase of 7.1% in the first quarter of 2017 after a 0.8% annual increase in the previous quarter, Q4 2016, according to DZS data.

The highest increase in turnover was recorded rental and leasing activities - 25.1%, travel agency, tour operator reservation services and related activities - 15.9% and computer programming, consultancy and related activities - 12.6%.

On the other hand, the highest decrease in turnover was recorded in publishing activities - 3.9%, real estate activities - 3.9% and motion picture, video and television programme production, sound recording and music publishing activities - 3.0%.

The wholesale sector went up by 4.4% y/y, following a 5.8% rise in Q4 2016.



Source: DZS

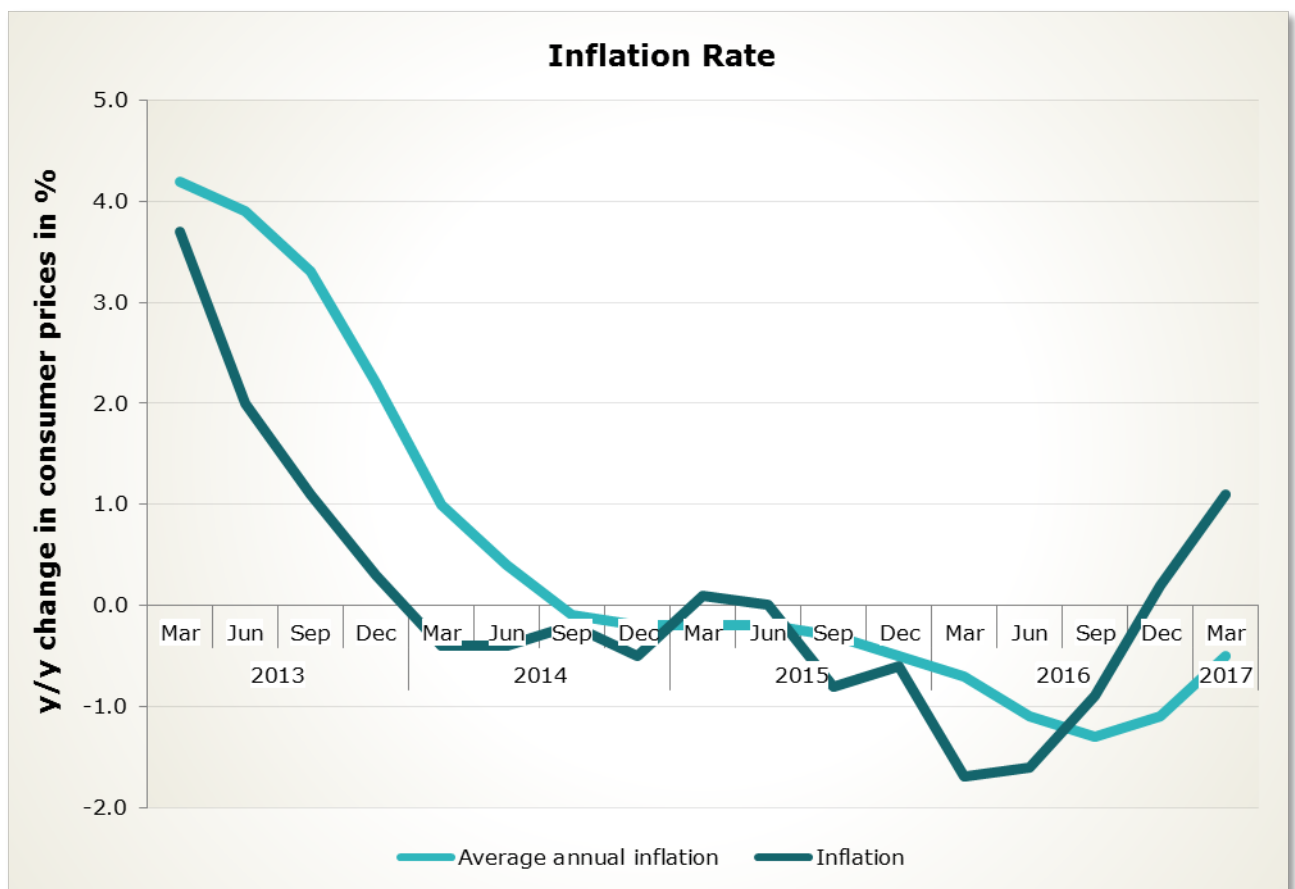
2.5. INFLATION

Average annual deflation of 0.5% as of March 2017

Consumer prices in Croatia went down by 0.5% in the period April 2016 – March 2017, compared to April 2015 – March 2016, according to DZS. This is a deflation slowdown compared to the whole 2016, when the average annual deflation was 1.1%.

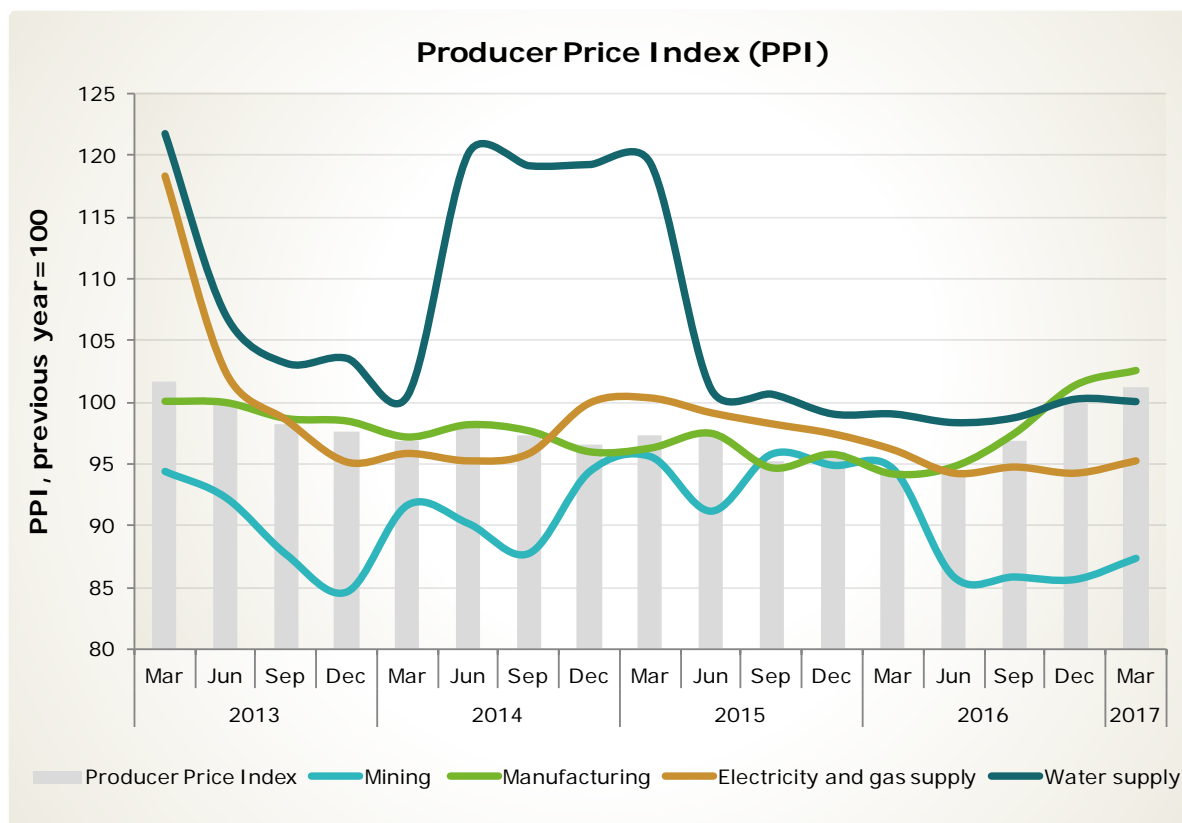
Headline inflation accelerated in March 2017 to 1.1% from 0.2% in December 2016 because of energy price contribution due to oil price surge on the international markets, which affected refined petroleum products.

In March 2017, as compared to February 2017, the average prices in Croatia increased by 0.3%, primarily as a result of the seasonal increase in the prices of clothing and footwear - 12.6%. On average, the monthly increase in the consumer prices in March 2017 was alleviated by a decrease of 0.8% in the prices of food and non-alcoholic beverages, of 0.7% in the prices of transport, and of 0.4% in the prices of Housing, water, electricity, gas and other fuels.



Source: DZS

Producer prices went up annually, by 1.2% in March 2017. Manufacturers producer prices inched up by 2.6% y/y, while the average producer prices in the mining sector went down by 12.6% y/y. The sector of electricity and gas supplies saw decrease of 4.8% y/y in producer prices, on average.



Source: DZS

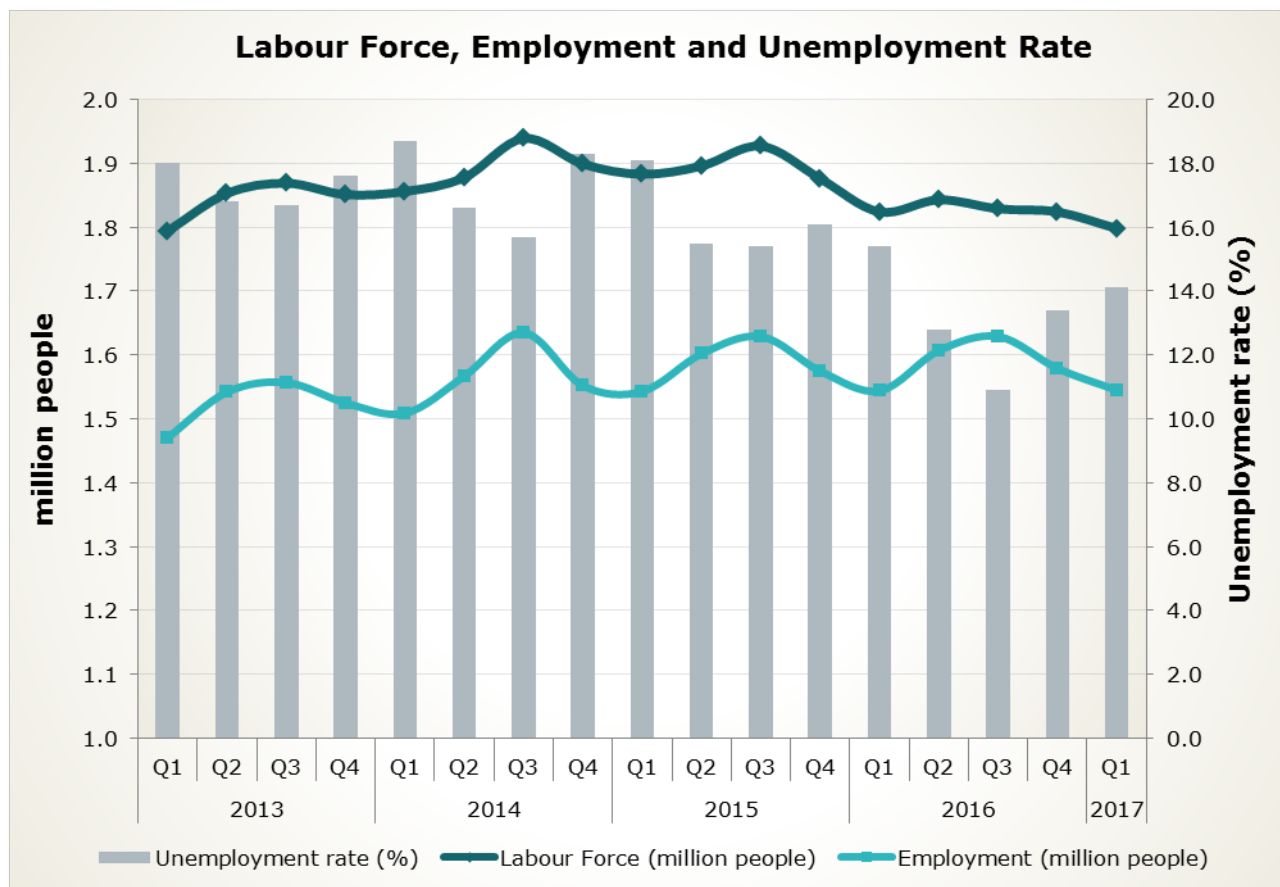
3. LABOUR MARKET

Unemployment rate went down y/y to 14.1%, wages grew 4.7% y/y as of March 2017

The favourable labour market developments that marked 2016 continued in the first three months of 2017. The unemployment rate in Croatia narrowed to 14.1% of the total labour force in Q1 2017 from 15.4% a year earlier, according to data of DZS.

The employed population aged 15 years and older was 1.545 million as of March 2017, up 0.1% y/y. Employment pickup was led by growth in the number of employed persons in industry and construction activities. However, youth unemployment remains high and increased to 34.4% in March 2017 from 32.5% a year earlier.

The average monthly net salary in January – March 2017 went up by 4.7% y/y to HRK 5,937, according to data of DZS. The growth in salaries was a result of the improving economic developments in Croatia and in part reflects problems of labour shortages in specific types of occupations.



Source: DZS

4. CONSTRUCTION AND REAL ESTATE

The number of building permits jumped by 41% y/y in Q1 2017

The number of permits for new buildings, excluding civil engineering, issued in Croatia in the first quarter of 2017 surged by 41% y/y and totalled 1,234, according to DZS data.

Permits for non-residential¹ buildings increased by 36% to 320, while permits for residential buildings registered a 43.3% increase to 914.

The total built-up area of the non-residential units, covered by the permits, increased by 21.7% y/y to 271,741 sq m. The total built-up area of the housing units went up by 66.4% to 346,164 sq m.

5. MONEY SUPPLY AND BANKING SYSTEM

5.1. HRK EXCHANGE RATE

The average quarterly exchange rate of the HRK against the EUR fell to HRK 7.4685 in Q1 2017 from HRK 7.6186 in Q1 2016, according to the Croatian National Bank (HNB).

Average Quarterly HRK Exchange Rate			
Foreign Currency	Q1 2017	Q4 2016	Q1 2016
EUR	7.4685	7.5168	7.6186
USD	7.0167	6.9615	6.9171
GBP	8.6870	8.6578	9.9032
CHF	6.9848	6.9614	6.9533

5.2. MONETARY POLICY

The national bank kept the policy rate unchanged at 3.0%

The HNB continued its expansionary monetary policy keeping the monetary policy rate at 3.0% and the liquidity of the domestic financial market held steady at a record high level. The average surplus liquidity stood at HRK 16.5 bln in March and the average weighted interest rate in inter-bank trade on the overnight market was at 0.02%. At the same time, the interest rate on one-year kuna T-bills without a currency clause dropped to its all-time low of 0.45%.

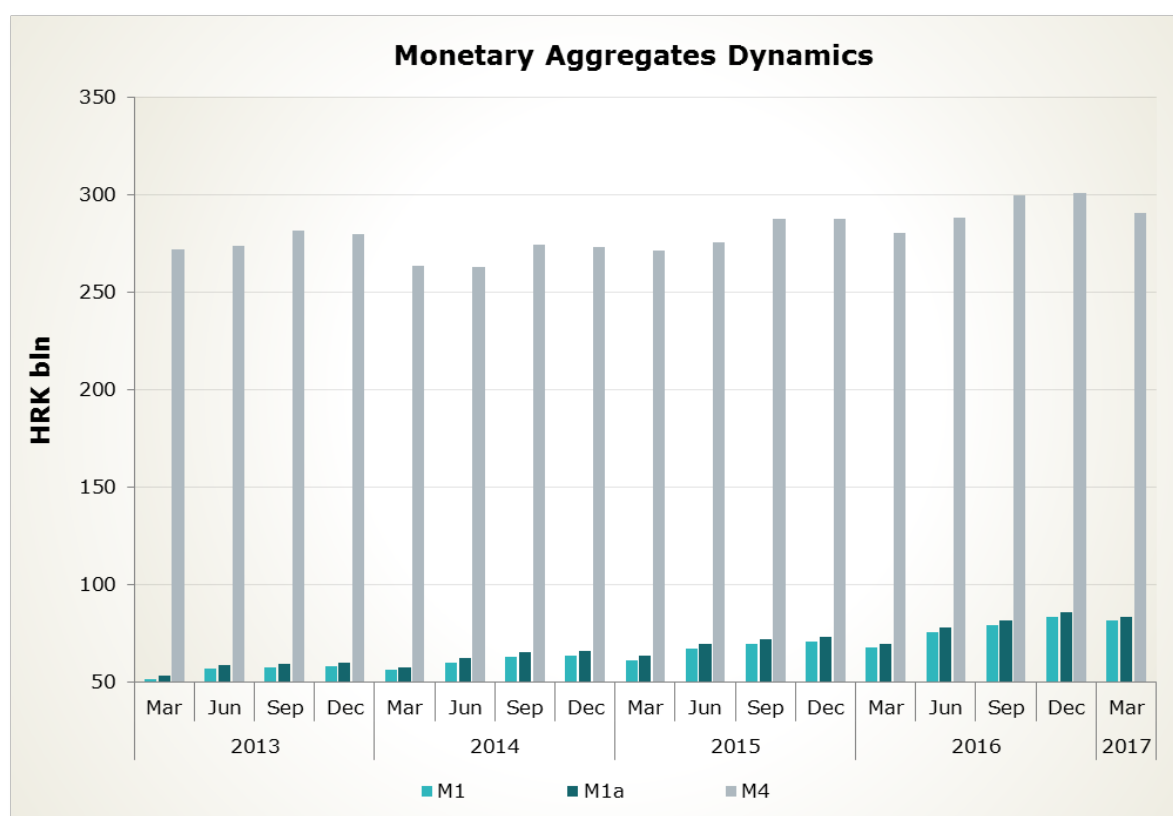
5.3. MONETARY AGGREGATES

Money supply growth was 3.7% y/y as of March 2017

¹ Non-residential buildings category includes: hotels, offices, wholesale and retail trade buildings, traffic and communication buildings, industrial buildings and warehouses, and public entertainment, education, hospital or institutional care buildings.

Broad money (money aggregate M4) increased by 3.7% y/y and reached HRK 290.92 bln in March 2017, according to data provided by HNB. The growth in money supply as measured by M4 slowed compared to the end of 2016 when M4 inched up by 4.7% y/y. According to HNB, the slowdown was achieved amid stronger growth, of 20.2%, in net foreign assets of monetary institutions and of a decline, of 3.5%, in net domestic assets of the monetary system. Net foreign assets increased because of the inflow of funds from a foreign bond issue to the government's foreign currency account with the HNB while the net domestic assets went down on increase in the government's foreign currency account.

The M1a² money aggregate rose by 20% to HRK 83.775 bln and money aggregate M1, or narrow money, also went up, by 21.1%, to HRK 81.845 bln.



Source: HNB

5.4. BANKING AND INSURANCE

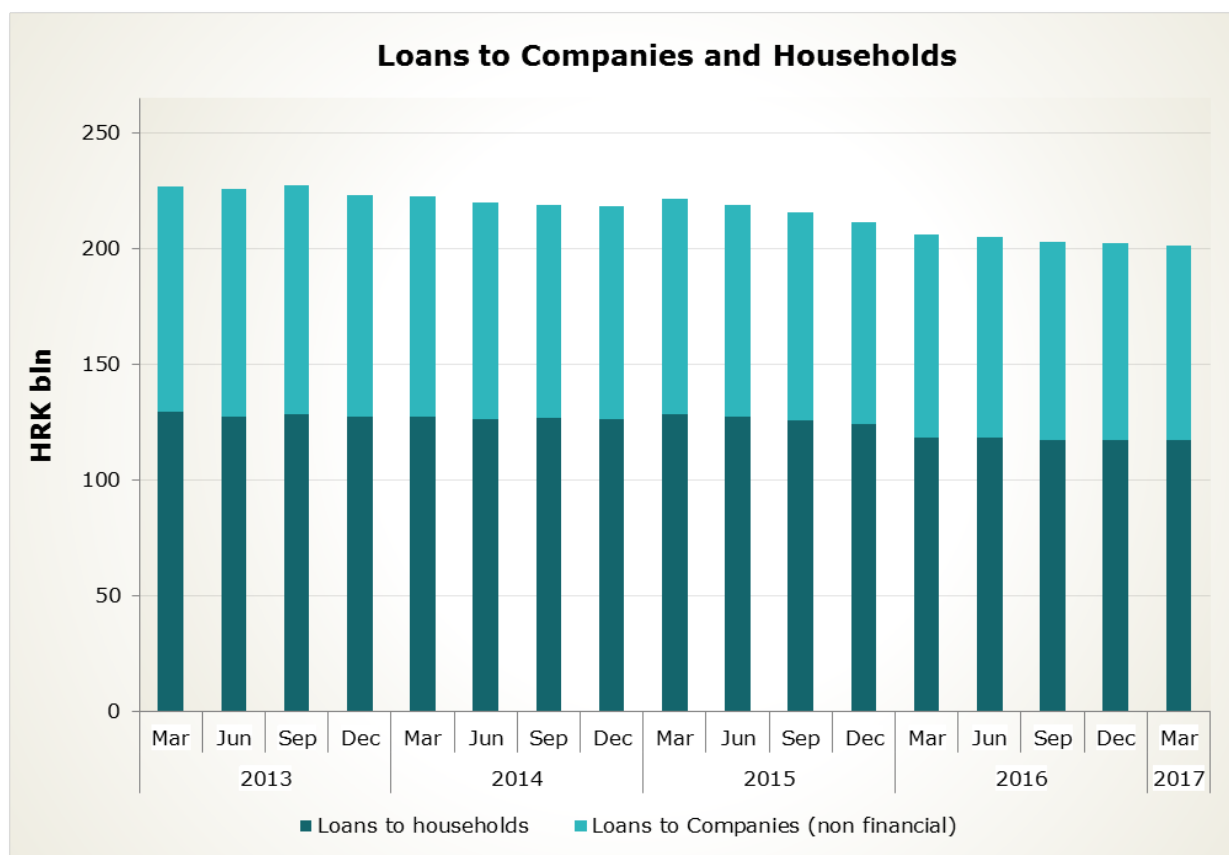
Household loans decreased, by 0.9% y/y in March 2017

Household loans went down by 0.9% to HRK 117.2 bln, according to HNB data. House purchasing loans narrowed by 2.7% to HRK 51.735 bln, accounting for 44% of the total loans.

² Money M1a comprises currency outside credit institutions and demand deposits with credit institutions, increased by the demand deposits of the central government with credit institutions.

The second largest loan type, slicing a 35% share, was the any-purpose cash loan with its value rising to HRK 41.2 bln from HRK 39.8 bln, according to HNB.

Loans to non-financial corporations went down by 4.1% y/y to HRK 84.4 bln.

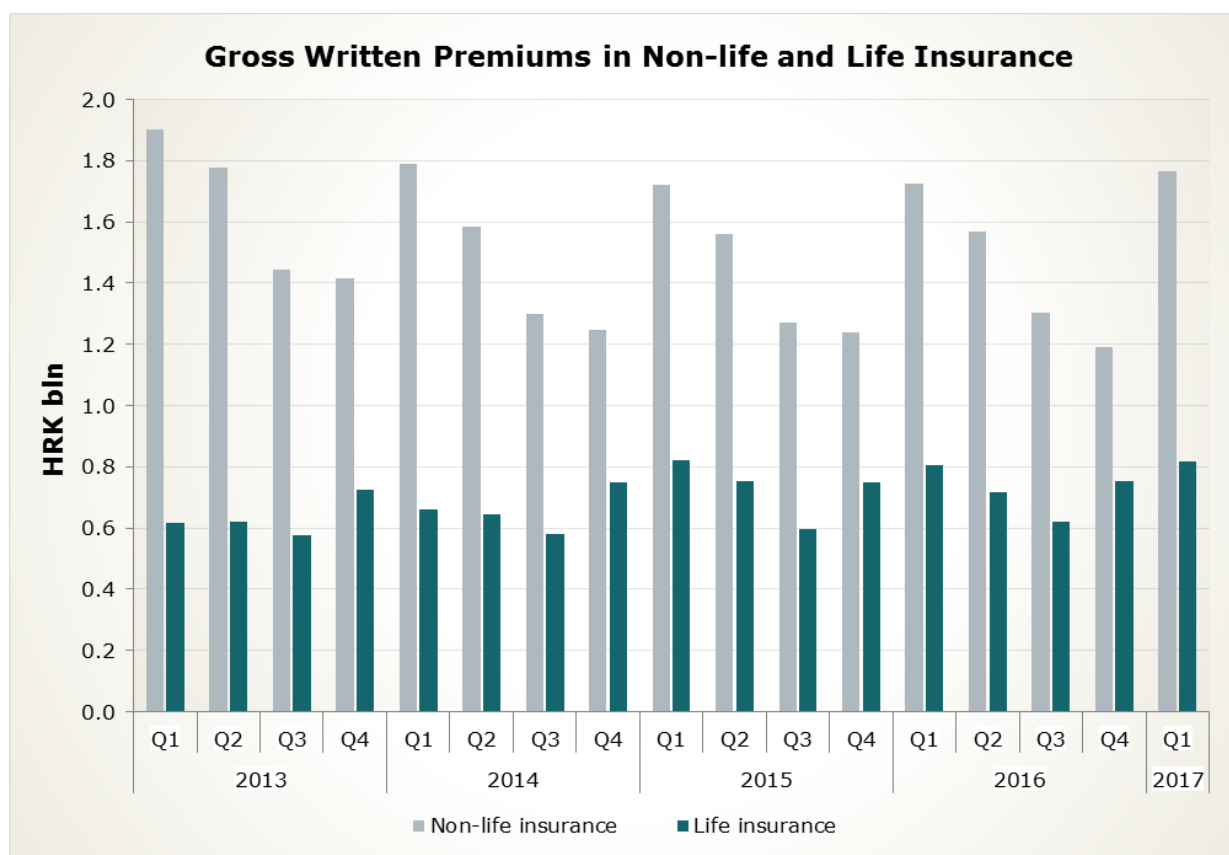


Source: HNB

Insurance premium income down 2.2% y/y in Q1 2017

The total gross written premiums (GWP) of the non-life and life insurance companies, excluding reinsurance, stood at HRK 2.586 bln, down by 2.2% y/y in Q1 2017, according to the Croatian Financial Services Supervisory Agency (HANFA).

The downtrend was due to the 3.9% annual decrease of the non-life insurance sector, which posted GWP of HRK 1.767 bln. The life insurance sector inched up by 0.6% y/y to HRK 819 mln.



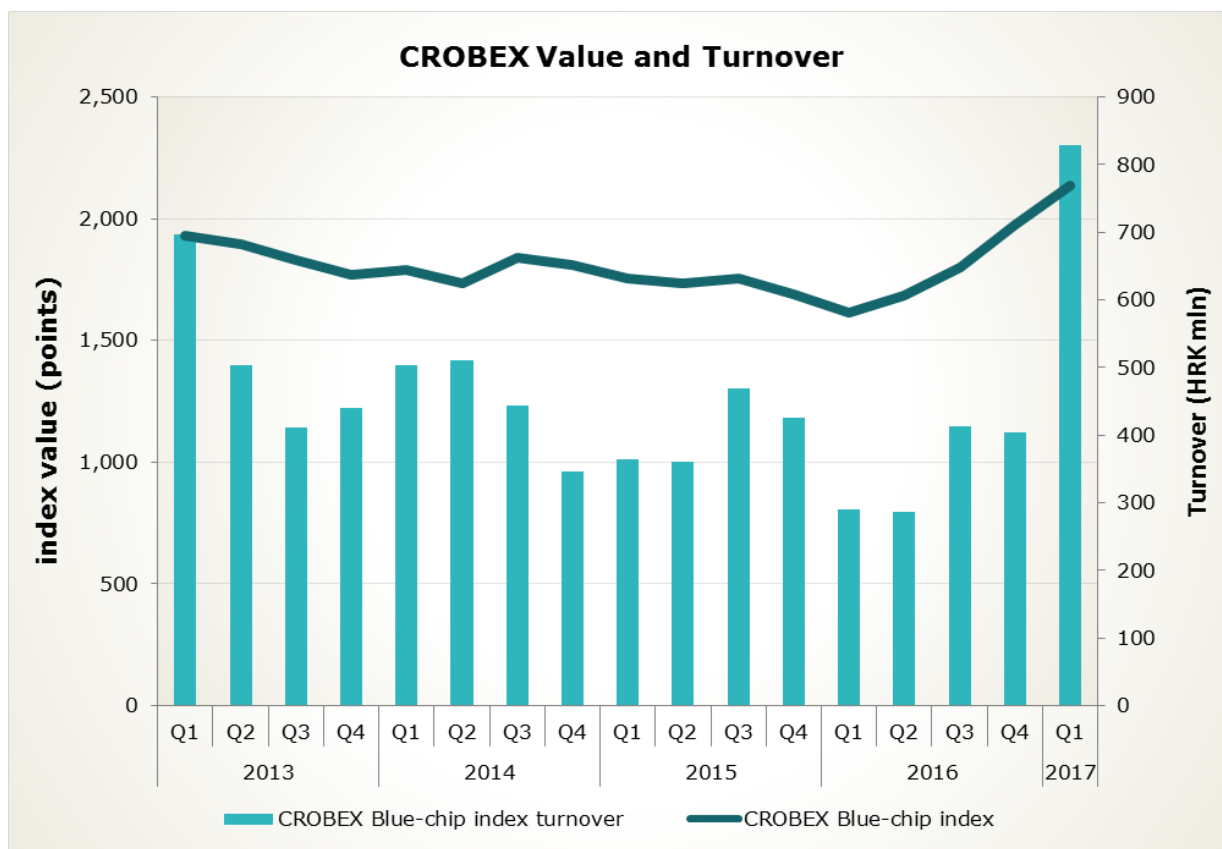
Source: HANFA

6. CAPITAL MARKETS

Blue-chip CROBEX up by 8.2% q/q in Q1 2017

The average value of CROBEX, the blue-chip index of the Zagreb Stock Exchange (ZSE), increased, by 8.2% q/q, to 2,137 points in Q1 2017.

The CROBEX turnover totalled HRK 828.0 mln in Q1 2017, compared to HRK 404.3 mln during the last three months of 2016.



Source: ZSE

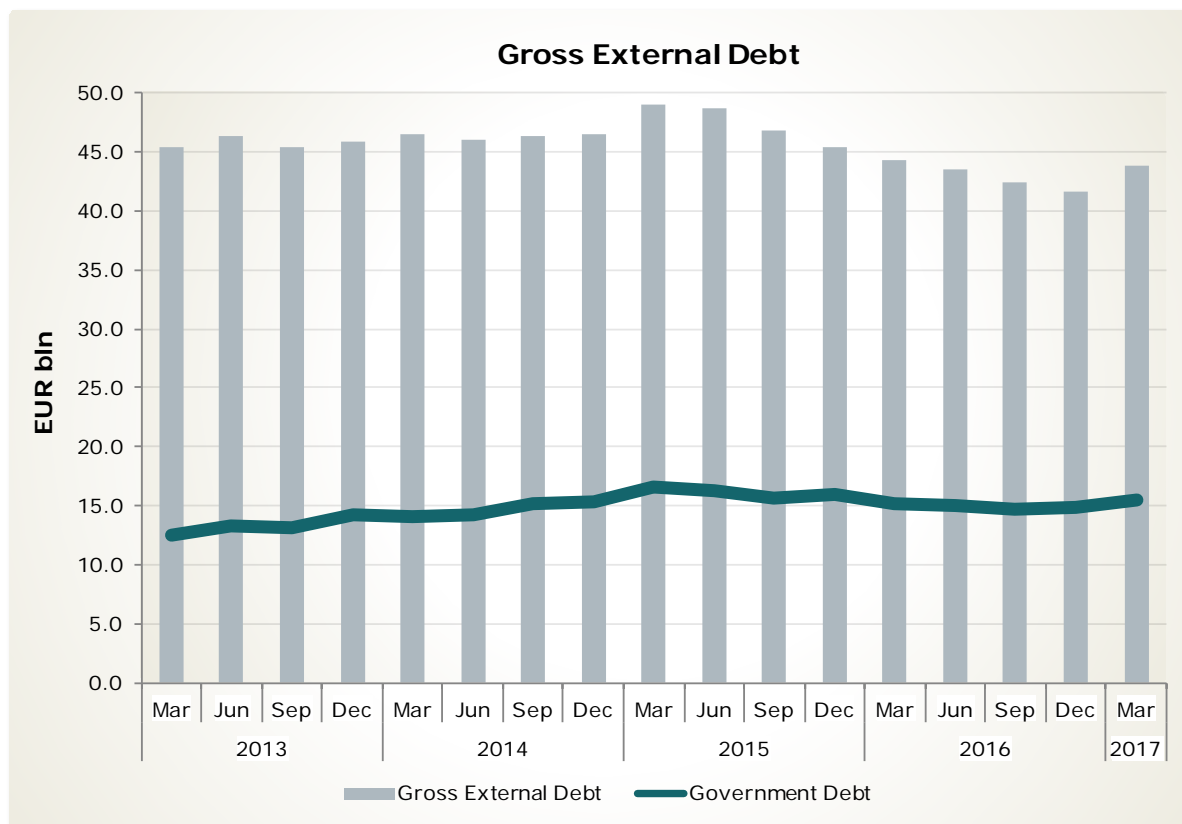
7. EXTERNAL SECTOR

7.1. FOREIGN DEBT

The gross external debt narrowed y/y to EUR 43.804 bln in March 2017

The gross external debt totalled EUR 43.804 bln as of March 2017, according to HNB. It went down by 1.1%, or EUR 479 mln, compared to March 2016.

As of March 2016, long-term liabilities amounted to EUR 32.707 bln, or 74.7% of the total debt, decreasing by 6.7% on the year. Short-term liabilities totalled EUR 5.312 bln, equal to 12.1% of the total debt and up by 56.6% compared to a year ago.



Source: HNB

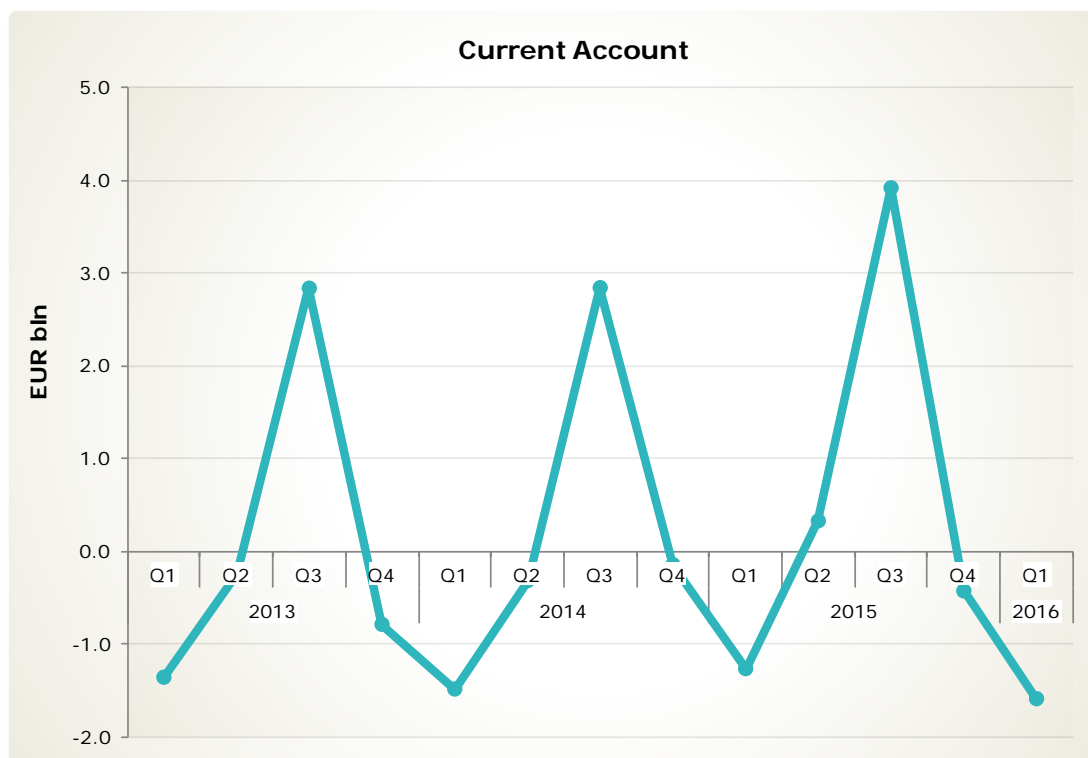
7.2. BALANCE OF PAYMENTS

Current account deficit at EUR 1.528 bln in Q1 2017

The current account deficit increased to EUR 1.528 bln in Q1 2017, up 2.6% y/y, according to central bank statistics data. In comparison to the previous quarter, Q4 2016, the deficit widened by EUR 848.9 mln. The current account of the balance of payments of Croatia is usually in a deficit in the first and the last quarter and in a surplus in the second and third as the country is a popular sea tourist destination.

The balance on the goods account was negative at EUR 1.978 bln, up 12.0% y/y, while services surplus went down by 11.0% y/y to EUR 336.5 mln.

The income account was positive during the first three months at EUR 113.8 mln compared to income gap of EUR 183.8 mln in Q1 2016.



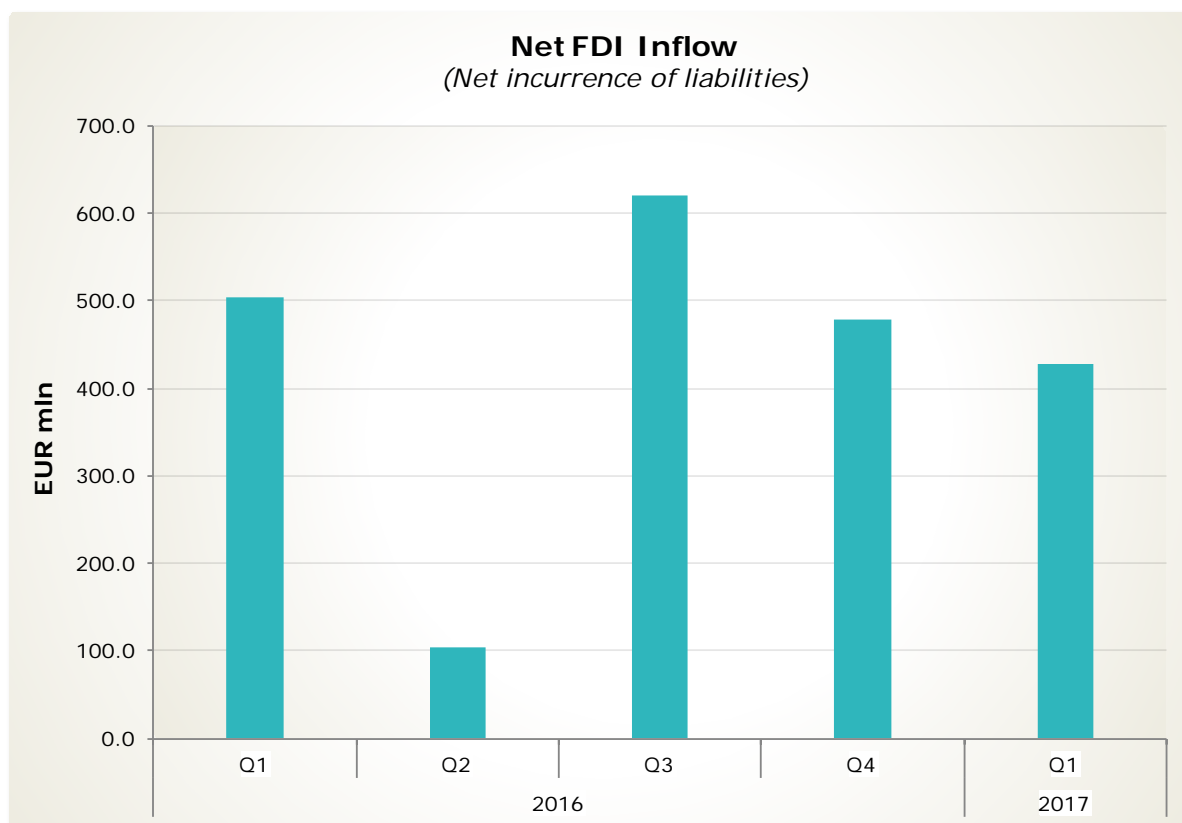
Source: HNB

7.3. FDI

Net FDI inflow at EUR 427 mln in Q1 2017

Net Foreign Direct Investments (FDI) inflow in Croatia totalled EUR 427 mln in Q1 2017, according to preliminary data of HNB. This is down 15% compared to a year earlier when FDIs amounted to EUR 503 mln.

Debt instruments investments amounted to EUR 159.5 mln, while net reinvested earnings inflow amounted to EUR 137.5 mln. Equity investments came in at EUR 130.1 mln.



Source: HNB

7.4. FOREIGN TRADE

Foreign trade deficit widens by 3.7% y/y in Q1 2017

The trade deficit stood at EUR 1.838 bln in Q1 2017, compared to EUR 1.773 bln in the corresponding quarter of the previous year, according to DZS.

Exports grew 25% y/y to EUR 3.362 bln, while imports increased by 16.5% on the year to EUR 5.2 bln. Import increased less than exports as a consequence of a decline in the imports of oil and refined petroleum products and ships.



Source: HNB

7.5. TOURSIM

Number of foreign tourist overnights decreased by 1.7% y/y in Q1 2017

Croatia is a popular sea tourist destination due to its long coastline on the Adriatic Sea. Tourist overnights of foreigners decreased by an annual 1.7% to 1.068 million in Q1 2017, according to DZS.

The total number of overnights, both of foreign and local tourists, reached 1.662 million, declining by 0.8% in comparison a year earlier.

The number of foreign tourists went up - by 2.3% y/y to 458,506.



Source: DZS

8. MAJOR DEVELOPMENTS

S&P affirms Croatia at 'BB/B', outlook stable

Mar 24, 2017

Standard & Poor's said on Mar 24, 2017 it has affirmed its 'BB' long-term and 'B' short-term foreign and local currency sovereign credit ratings on Croatia, with a stable outlook.

[Read the full story here](#)

Bulgaria, Croatia, Romania meet EU 2020 renewable energy in consumption target in 2015

Mar 14, 2017

Bulgaria, Croatia and Romania have met in 2015 their target share of energy from renewable sources in gross final consumption of energy, as set out in the Europe 2020 strategy, announced the European Commission.

[Read the full story here](#)

Croatia burdened by excessive imbalances, makes little progress on reforms – EC

Feb 22, 2017

The European Commission (EC) said on Feb 22, 2017 that Croatia is experiencing excessive imbalances linked to high levels of public, private and external debt in a context of low potential growth. [Read the full story here](#)

EIB to focus on catalysing private capital in Croatia

Feb 22, 2017

The European Investment Bank (EIB) said on Feb 22, 2017 it will focus on catalysing private capital and implementing projects entailing higher risks in Croatia in the coming years. In 2016, the EIB signed loans totalling EUR 530 mln in Croatia, 50% more than a year earlier, the lender said in a statement.

[Read the full story here](#)

EIF, PBZ unlock EUR 47 mln in loans to Croatian SMEs

Feb 21, 2017

The European Investment Fund (EIF) and Privredna banka Zagreb (PBZ) have signed an agreement that will unlock HRK 350 mln (EUR 47 mln) worth of loans to small and medium-sized enterprises (SMEs) in Croatia, according to the European Commission.

[Read the full story here](#)

Croatia to spend EUR 200.9 mln to boost employment

Feb 9, 2017

Croatia's government said on Feb 9, 2017 it plans to direct HRK 1.5 bln (EUR 200.9 mln) into measures for stimulating employment, particularly of young and long-term unemployed people.

[Read the full story here](#)

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