

Finally out of recession

General Information



GDP	USD57.2bn (World ranking 78, World Bank 2014)
Population	4.2mn (World ranking 127, World Bank 2014)
Form of state	Parliamentary Democracy
Head of government	Tihomir ORESKOVIC (prime minister)
Next elections	2019, presidential and legislative



Strengths

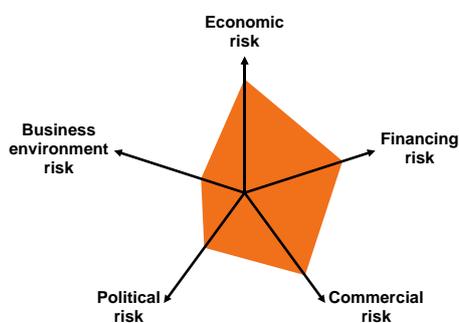
- Good international relations; EU membership
- Exchange rate stability thanks to "managed float"
- Current account surpluses since 2013

Weaknesses

- Vulnerability to EU business cycle
- Ongoing private sector credit contraction as a result of bank deleveraging
- Persistent deflation since early 2014
- Rapidly deteriorating public finances have resulted in sovereign downgrades to speculative grade in 2012-2013
- Very high external debt
- Considerable refinancing risk of companies and banks

Country Rating

C3



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports	Rank	Imports
Italy	13%	14%
Slovenia	13%	13%
Bosnia and Herzegovina	12%	11%
Germany	9%	8%
Serbia	7%	7%

By product (% of total)

Exports	Rank	Imports
Refined Petroleum Products	9%	8%
Pharmaceuticals	5%	7%
Non-Edible Agricultural Prod.	4%	4%
Miscellaneous Hardware	4%	4%
Electricity	4%	4%

Source: Chelem (2014)

Economic Overview

Returning to growth

After six consecutive years of annual GDP contraction, the economy returned to growth of +1.6% in 2015, thanks to a moderate recovery in domestic demand. Private consumption increased by +1.2%, government consumption by +0.6% and fixed investment by +1.6%. Exports expanded by +9.2%, outpacing imports at +8.6%, so that net exports made a positive contribution of +0.5ppps to growth in 2015. Euler Hermes expects the recovery to gradually gain momentum, resulting in growth of about +1.8% in 2016 and +2% in 2017. However, the level of annual GDP will remain about -10% below the peak reached in 2008.

Economic policies need to improve

Monetary policy is based on a “managed” exchange rate float which has helped insulate the economy from overly inflationary pressures in the past. The HRK has faced frequent downward pressure in recent years but ongoing central bank intervention in foreign exchange (FX) markets have kept the HRK/EUR exchange rate fairly stable, albeit at the expense of broadly stagnating FX reserves. Current FX reserves cover just about 62% of the estimated external debt payments falling due in the next 12 months which is below an adequate level of at least 100%. Meanwhile, consumer price inflation has been in deflationary territory for almost two years owing to ongoing low global energy prices. Once the latter start rising again, we expect inflation to pick up as well.

The extended recession has weakened public finances. Despite fiscal consolidation efforts, fiscal deficits have remained large (about -5% of GDP in 2015) and public debt has risen rapidly from 34% of GDP in 2007 to 90% or so in 2015. Euler Hermes expects the fiscal deficit to narrow somewhat in 2016 but unlikely to meet the less than -3% of GDP target required by the EU's Excessive Deficit Procedure. However, external financing conditions have remained manageable thus far as Croatia has been able to issue several international bonds since 2013.

Mixed external position

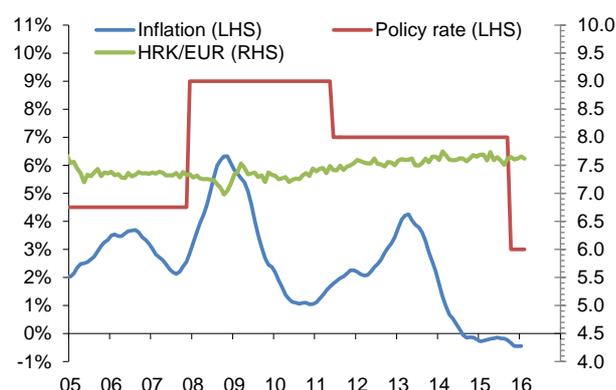
The current account has been in surplus since 2013, surging to about +4.5% of GDP in 2015, and should remain so in 2016-2017. However, total external debt remains very high (108% of GDP in 2015), a result of the legacy of large current account deficits in the past. The external debt-service ratio is hefty, forecast at over 44% in 2016, reflecting huge debt amortisation obligations that are likely to constrain financing for private investment.

Key economic forecasts

	2014	2015	2016f	2017f
GDP growth (% change)	-0.4	1.6	1.8	2.0
Inflation (% end-year)	-0.5	-0.6	1.0	1.5
Fiscal balance (% of GDP)	-5.6	-5.0	-4.8	-4.5
Public debt (% of GDP)	85.1	90.0	91.5	92.0
Current account (% of GDP)	0.8	4.5	3.0	2.5
External debt (% of GDP)	108.7	107.8	110.0	105.0

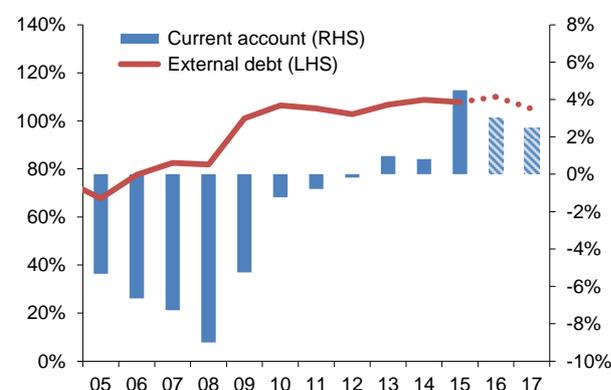
Sources: National sources, IHS, Euler Hermes

Inflation rate (12-month moving average, %), monetary policy interest rate (%), and exchange rate



Sources: National sources, IHS, Euler Hermes

Current account and external debt (% of GDP)



Sources: National sources, IHS, Euler Hermes

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