CROATIA: MACRO OUTLOOK

# Stage set for another solid year

Alen Kovac
Economy Croatia - Analyses and Forecasts | Erste Group Bank AG
December 13, 2024

Spot Rates as of: December 13, 2024
Note: Information on past performance is not a reliable indicator for future performance.
Forecasts are not a reliable indicator for future performance.

# Main message

Fresh GDP data confirmed that the solid economic momentum extended into 2H24 **(3Q GDP at 3.9% y/y)**, as growth remained dominated by the strong domestic demand. **Looking into 2025, the outlook remains solid, with GDP growth anticipated to moderate only slightly to around 3%.** The growth mix continues to point to steady domestic demand support, reflecting disposable income gains on the consumption side and still strong EU backing on the investments side. External demand is seen delivering only modestly stronger support, but it remains a risk to the forecasts amid ongoing uncertainties related to EA recovery dynamics.

**Following moderation and inflation averaging just below 3% in 2024, a similar print is expected for 2025.** Growth dynamics are pointing to ongoing domestic demand pressures, while supply side factors are seen keeping a relatively steady trajectory.

**Recent budgetary documents signaled that the MoF is targeting a 2024 budget gap closer to 2% of GDP (vs. 2.6% of GDP earlier). Also, the 2025 budget draft is eyeing a budget gap at similar levels (2.3% of GDP)** ,suggesting that the 2024 election-driven deterioration of the fiscal stance has not been a one-off and the cabinet is content with a somewhat looser fiscal stance. Despite less room for maneuver, we see the budget remaining within the EDP limits and public debt continuing to trend slowly down, further away from the 60% mark. **After Moody's delivered a surprising two-notch rating upgrade, we see rating agencies remaining on hold in 2025 as the most likely baseline.** Yields are back below 3% after a while, reflecting overall general market developments and anticipation of the ECB cutting towards 2% (or below) in 2025, and spread tightening closer to 80bp, amid supportive local specifics. Spread levels within 80-90bp on the long end should prevail in 2025.

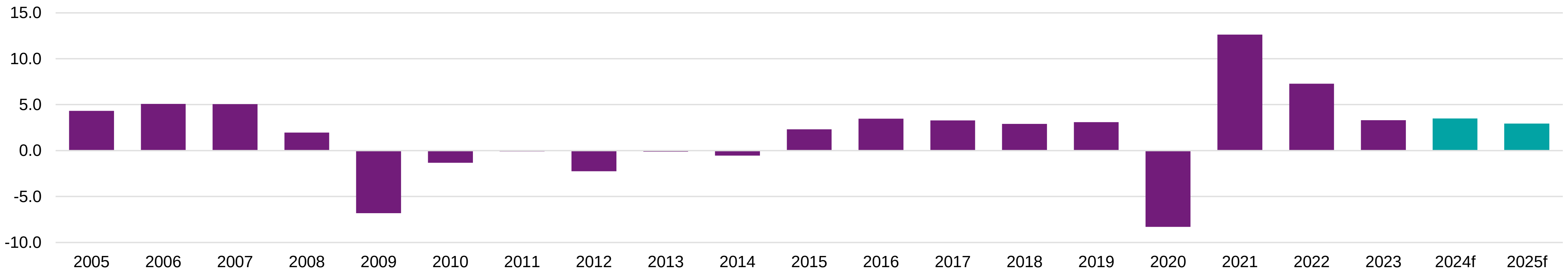


Source: Eurostat, Refinitiv, Erste Group Research

# GDP growth

**We expect the last quarter to wrap up FY24 GDP growth in the region close to 3.5%**, thus affirming another strong year, especially comparatively looking at the EU average in the sub-1% region. **Growth should get most of the support from domestic demand, remaining the driving force in 2025, though expected at more moderate levels.** Fundamentals on the labor market side remain supportive, but wage growth is anticipated to moderate back to the single-digit region, while employment gains are also seen softening after strong gains this year; hence, disposable income growth, while remaining supportive, should lose some steam next year. Considering potentially more cautious consumers, given the increasing global uncertainty, we are expecting private consumption growth to moderate back to the 3-4% region in 2025. A similar trajectory is expected on the investment side. EU fund flows and a still potent construction sector remain a tailwind, but increasing uncertainties related to external demand, despite the ECB starting to reverse the rate cuts, may weigh on the private sector, like the quite strong base effect, following the robust investment profile in the last couple of years. The external demand outlook remains relatively gloomy, and the anticipation of more supportive external demand is less of a baseline scenario at present. Apart from weighing on merchandise exports, the tourism outlook is getting more conservative, as 2024 confirmed the sector's struggle to surpass pre-pandemic overnight levels. **All things said, we see 2025 growth remaining in decent gear at around 3%, with risks more tilted somewhat to the downside, owing to global geopolitical uncertainties and lasting EU growth weakness.**

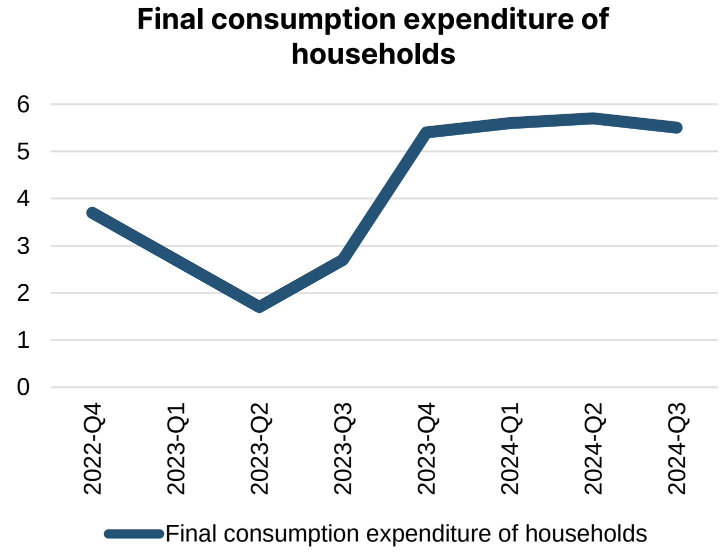
GDP growth, percent

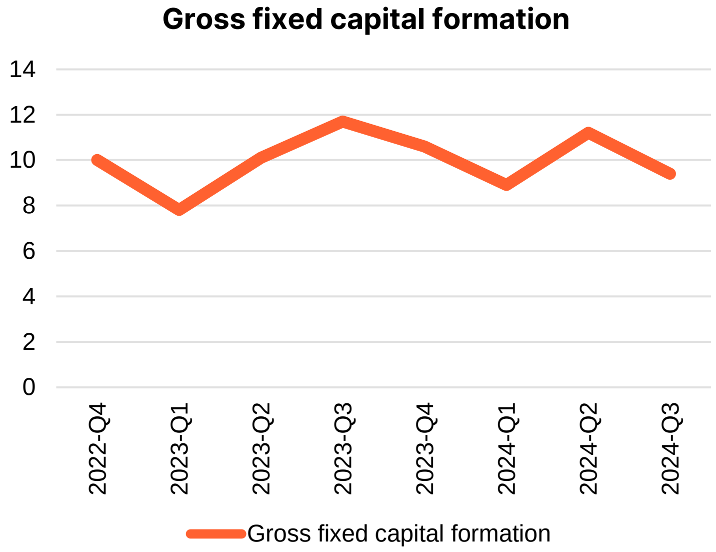


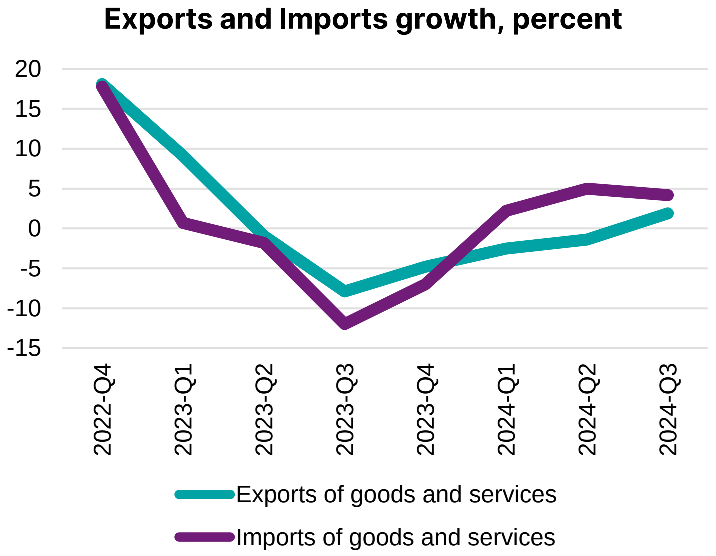



Source: Eurostat, Refinitiv, Erste Group Research
December 13, 2024

# GDP structure



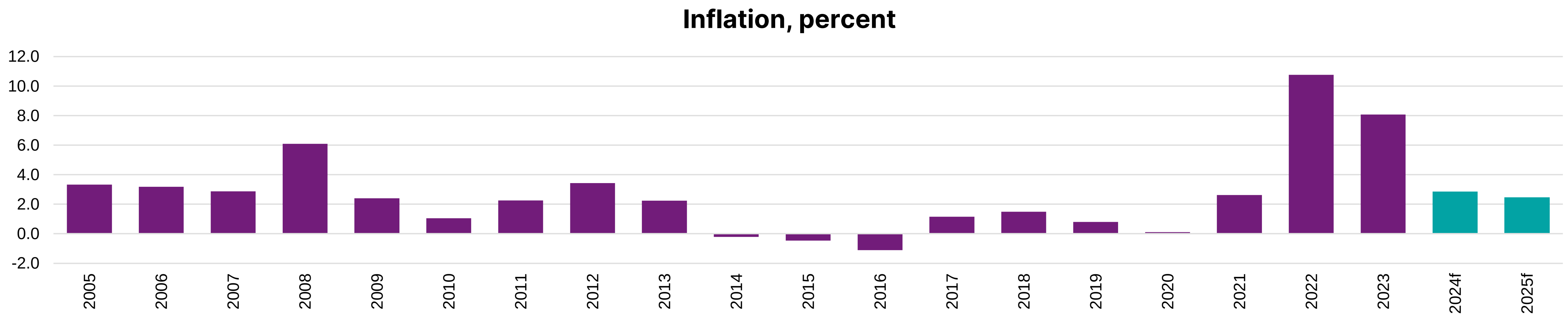




As anticipated, **GDP maintained a strong growth pace in 3Q24, with the headline figure accelerating to 3.9% y/y.** Looking at the seasonally-adjusted data, the q/q economy added a solid 0.8%, translating into 4.1% y/y. The detailed structure revealed that the strong domestic demand momentum continued, as private consumption remained vivid with a 5.5% y/y increase, while investment activity delivered another robust performance (9.2% y/y). Public consumption also moved to a higher gear with a 5.3% y/y increase. On the external trade side, we saw further normalization of the exports, as the figure brought a rebound at 1.5% y/y, driven by the goods performance (6.3% y/y), while once again services were in the red (-1.8% y/y, albeit with a milder decline than that seen in 2Q24). Imports were up 4.1% y/y, reflecting solid increases in both goods and services and being shaped by strong domestic demand. However, with import growth outpacing the export increase, the net export contribution had a less favorable impact on the headline figure in 3Q24.

# Inflation

After bottoming out in 3Q (1.6% y/y in Sep-24), 4Q saw inflation trending higher, with the **Nov-24 print hitting 2.8% y/y**, mostly owing to less supportive food price developments and electricity and natural gas price hikes. On the annual level, despite moderating pressure in recent months, services kept the strongest dynamic (+5.1% y/y), albeit with food prices converging (+4.6% y/y) and energy prices losing deflationary momentum (-0.4% y/y). **December CPI should wrap up the FY24 average just shy of 3%, while the outlook for 2025 suggests a figure remaining in the same ballpark.** Demand-side pressures should persist, but fade to an extent, as domestic demand is expected to shift into lower gear. The beginning of the year should bring an additional bump to energy prices (an additional approx. 3.5% hike to regulated electricity and natural gas prices), while the current baseline for 2025 envisages supply-side pressure remaining largely in check. Global political tension and heightened uncertainty remain the upside risks to the inflation outlook in case of renewed supply-side pressure.

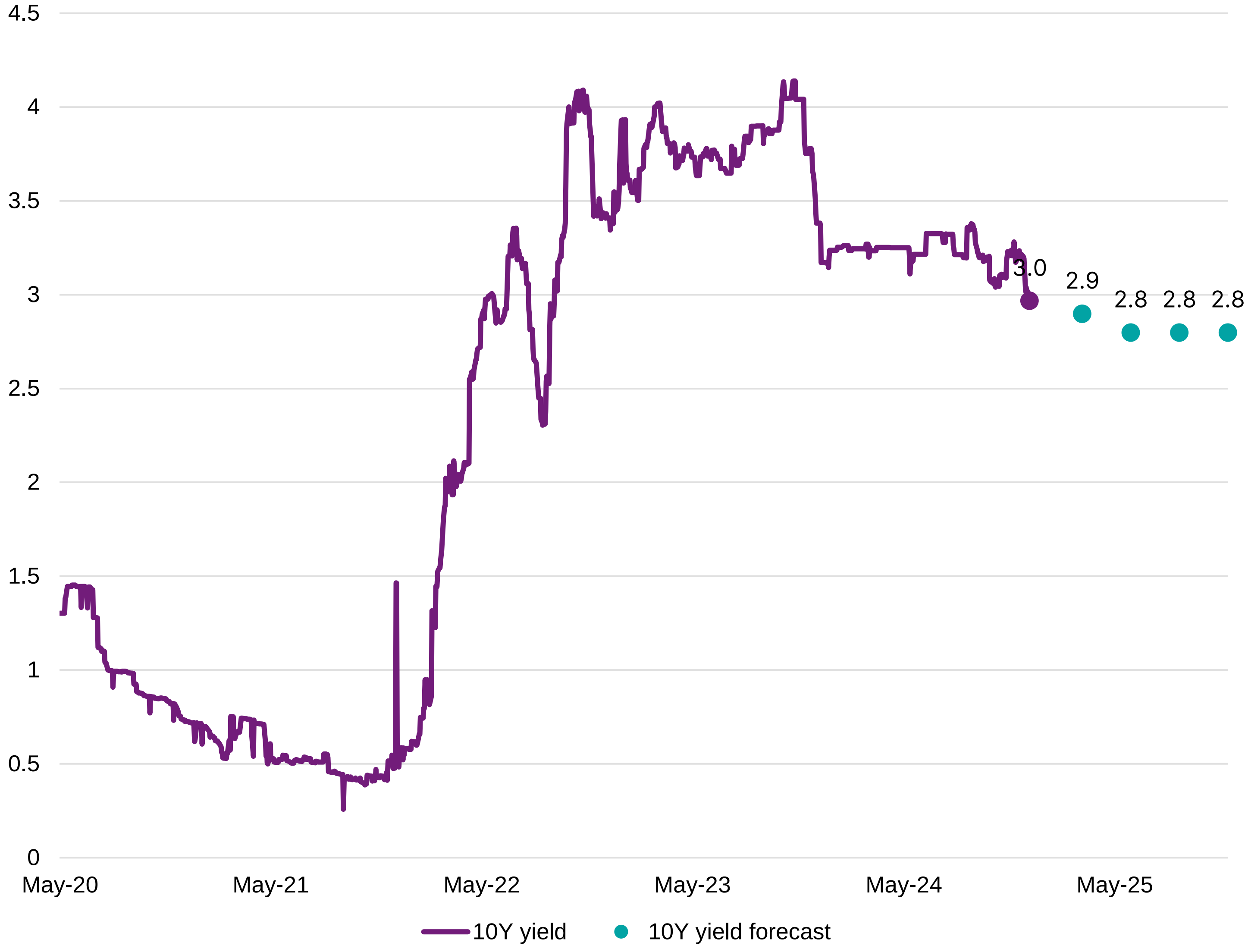



Source: Eurostat, Refinitiv, Erste Group Research

# Yields and spreads

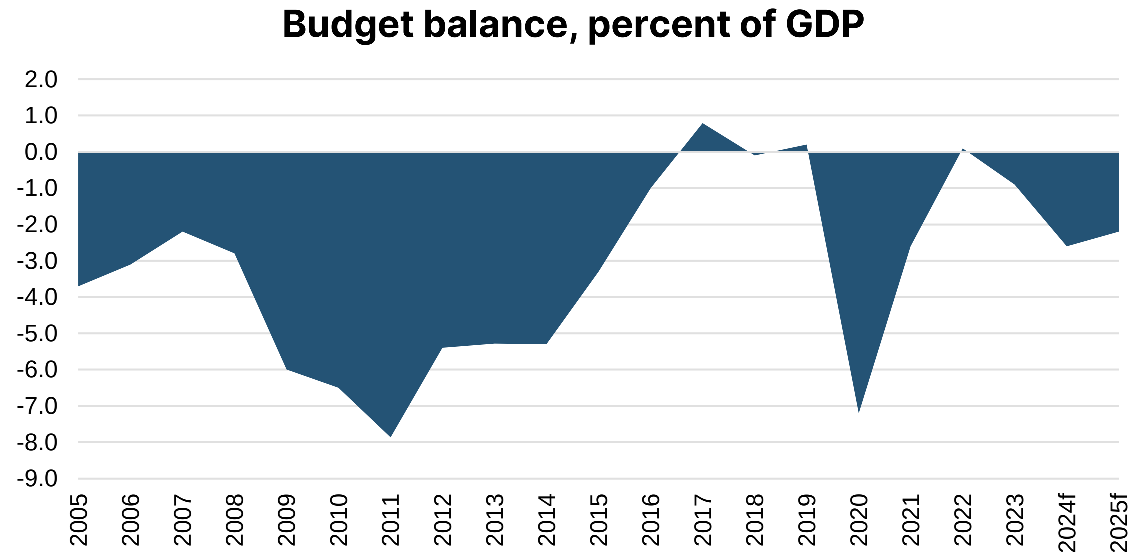
Starting with rating news, **Moody's delivered a two-notch rating upgrade ('A3', stable) in the last rating action in 2024**, thus aligning with S&P and Fitch at the 'A-' equivalent level. While we expected a move from Moody's, the two-notch move came as a bit of a surprise, especially given that we saw no big change in the rating drivers since the last assessment. Looking at the Ministry of Finance's financing actions, retail-targeted issuance remained in focus, with a volume of EUR 1.6bn expected in 4Q (EUR 1.2bn in Nov-24 and EUR 0.4bn in Dec-24). Looking at the maturity profile and with almost EUR 5.5bn maturing in 1Q25, the beginning of the year should bring more action. Looking at the yields, the 10-year rate (EUR 2034) until recently showed, by today's standards, a steady trajectory moving close to 3.1%, with volatility being mostly shaped by the developments in DE yields. With recent repricing and the benchmark moving closer to 2%, the HR 10-year rate saw a move down to the sub-3% region (currently around 2.9%) for the first time in more than two years. **We expect spreads to remain in the 80-90bp region in 2025, as the compression potential to peers has largely materialized.** Benchmark yields remain the shaping force as far as yield levels are concerned, hence with the DE 10-year rate seen moving close to 2% in 2025, the HR 10-year rate is seen remaining close to current levels.

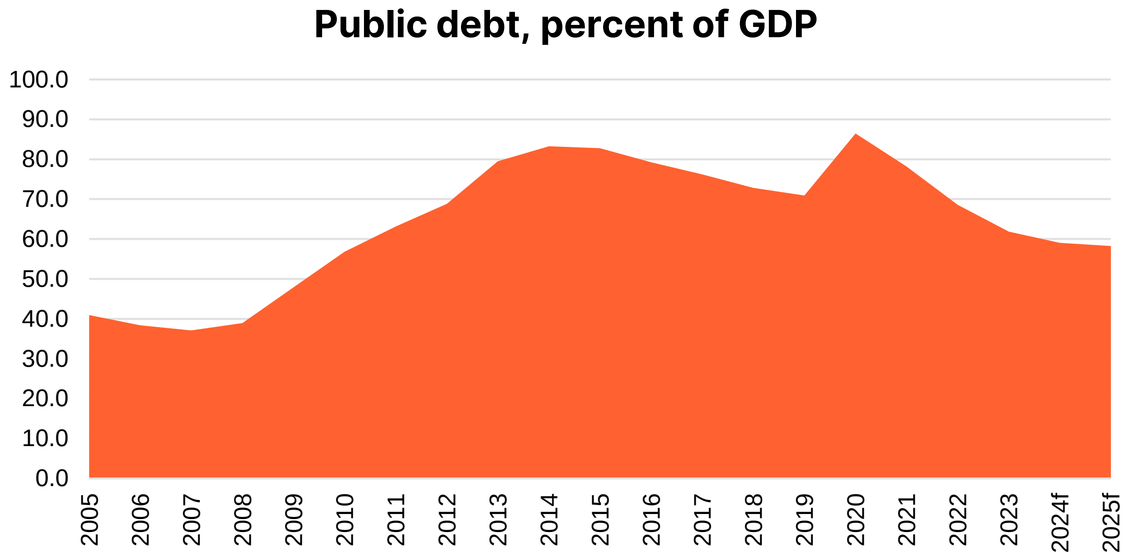
## 10Y yield development and forecast




Source: Eurostat, Refinitiv, Erste Group Research

# Fiscal Situation




With a new term secured, the 2025 budget draft has been the cabinet's first fiscal policy trajectory checkpoint. First, just to wrap up 2024, after bumping the deficit target to 2.6% of GDP (from 1.9% of GDP), the **MoF is now signaling it sees the budget gap closer to the initial target (2.1% of GDP).** However, we lack more concrete details, as in this iteration, the 2024 budget figures were left unchanged. **Going from there, the 2025 budget target is set at 2.3% of GDP.** Whether this is an improvement or deterioration depends on the which figure for 2024 we refer to, but it is fair to say that the MoF is targeting the gap at a very similar level as in 2024. **While in relation to CEE, Croatia remains in the diligent group, the 2025 budget confirmed that the departure in 2024 from a more balanced fiscal policy remains the course in 2025 as well.** Budgeting assumptions are also signaling less maneuvering space if the economy and revenue side were to under-deliver; hence, we see 2025 as no consolidation effort, but more of a muddling-through approach. However, public debt slipping below 60% of GDP already in 2024 and further gradual progress in the mid term, along with staying outside of the EDP zone, remains a reassuring trajectory as far as investor confidence is concerned.

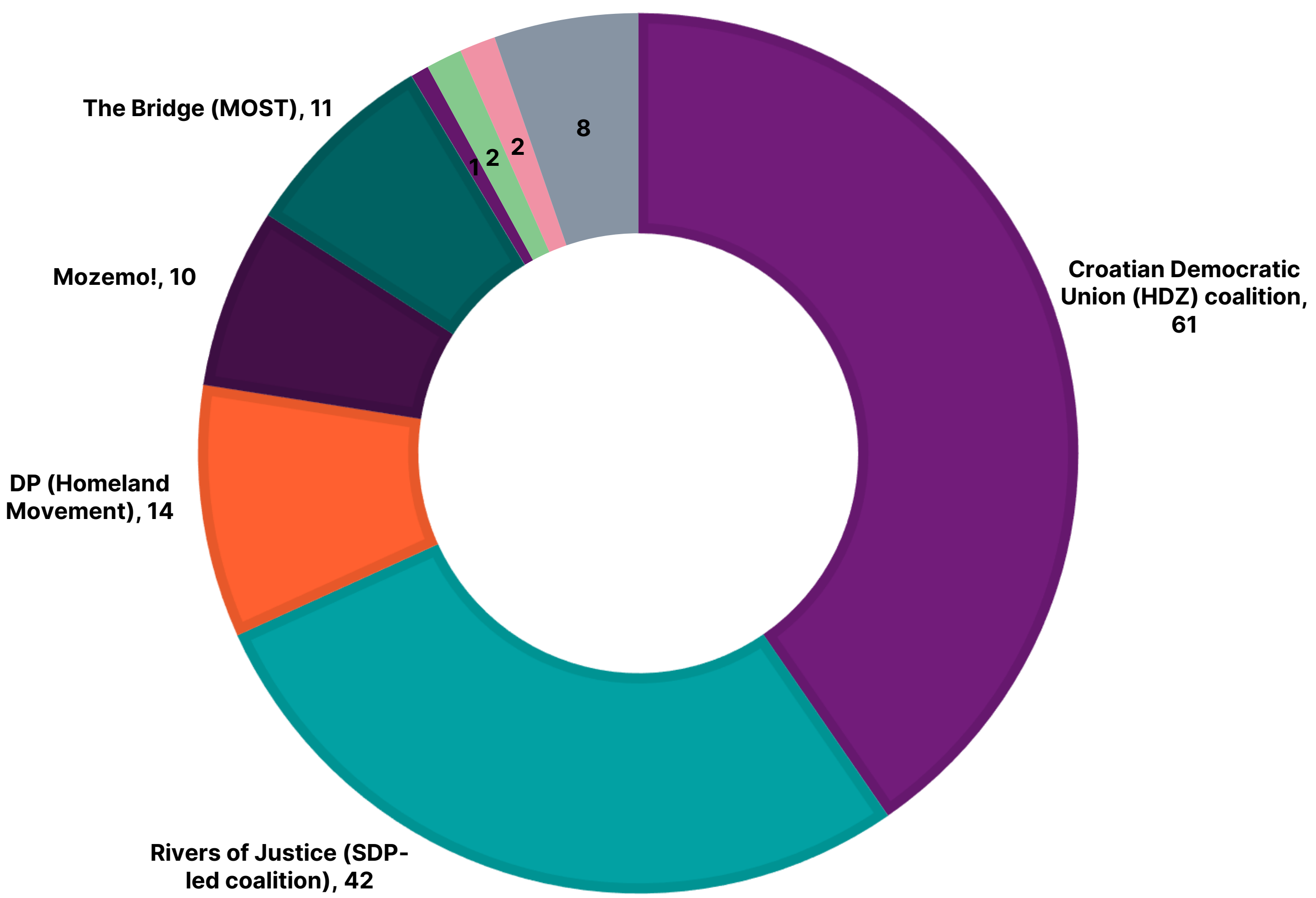
Source: Eurostat, Refinitiv, Erste Group Research

# Political landscape

In the super-electoral 2024, dessert, in the form of presidential elections, will be served late, as the first round is scheduled for December 29. If the polls are accurate, incumbent President Milanovic is likely to be reelected. Recent polls show that center-left candidate Milanovic is the front-runner with support within 37-38%, giving him a considerable advantage over ruling HDZ candidate Mr. Primorac, who enjoys slightly over 20% support. Independent (center-right) candidate Mrs. Selak Raspudic and leftist candidate Mrs. Kekin are scoring support close to 10%, rounding out the list of candidates with double-digit or close to double-digit support. While a first-round victory is not out of the question, in a potential run-off, Milanovic is looking comfortable, with solid support across the electorate and the potential to sway votes from candidates dropping out of the race.

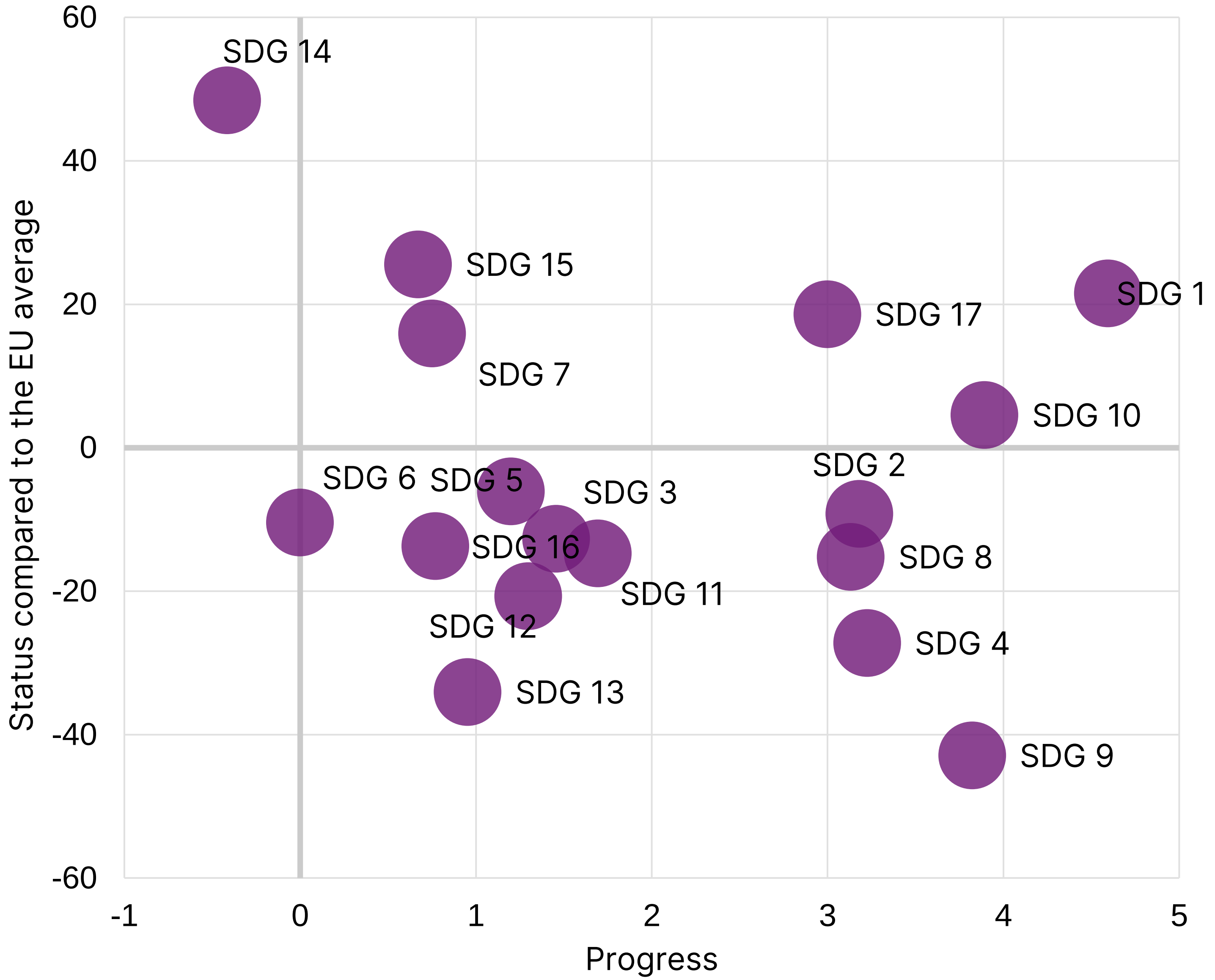
As far as parliament is concerned, a government with a relatively thin yet stable majority remains the baseline. This has been confirmed by a recent unsuccessful no-confidence vote. The risk of early elections remains low.

## Parliamentary seats




Source: Eurostat, Refinitiv, Erste Group Research

# Social Development Goals




Regarding SDGs, Croatia is showing an improving trend for the vast majority of them. Croatia scores above average in 6 out of 17 SDGs and apart from SDG 14 (Life below water) is showing further progress. Out of 11 SDGs that are ranked below the EU average, significant progress is being made in 4 of them - Zero hunger (SDG 2), Quality education (SDG 4), Decent work and economic growth (SDG 8) and Industry, innovation and infrastructure (SDG 9). Regarding other below-average SDGs – Clean water and sanitation is showing no progress at the moment, while remaining SDG are showing gradual improvement. Looking at the gap to EU average Industry, innovation and infrastructure (SDG 9), Climate action (SDG 13) and Quality education (SDG 4) should remain in the focus.

Source: Eurostat, Refinitiv, Erste Group Research

# Dwelling on sovereign financing needs for 2025

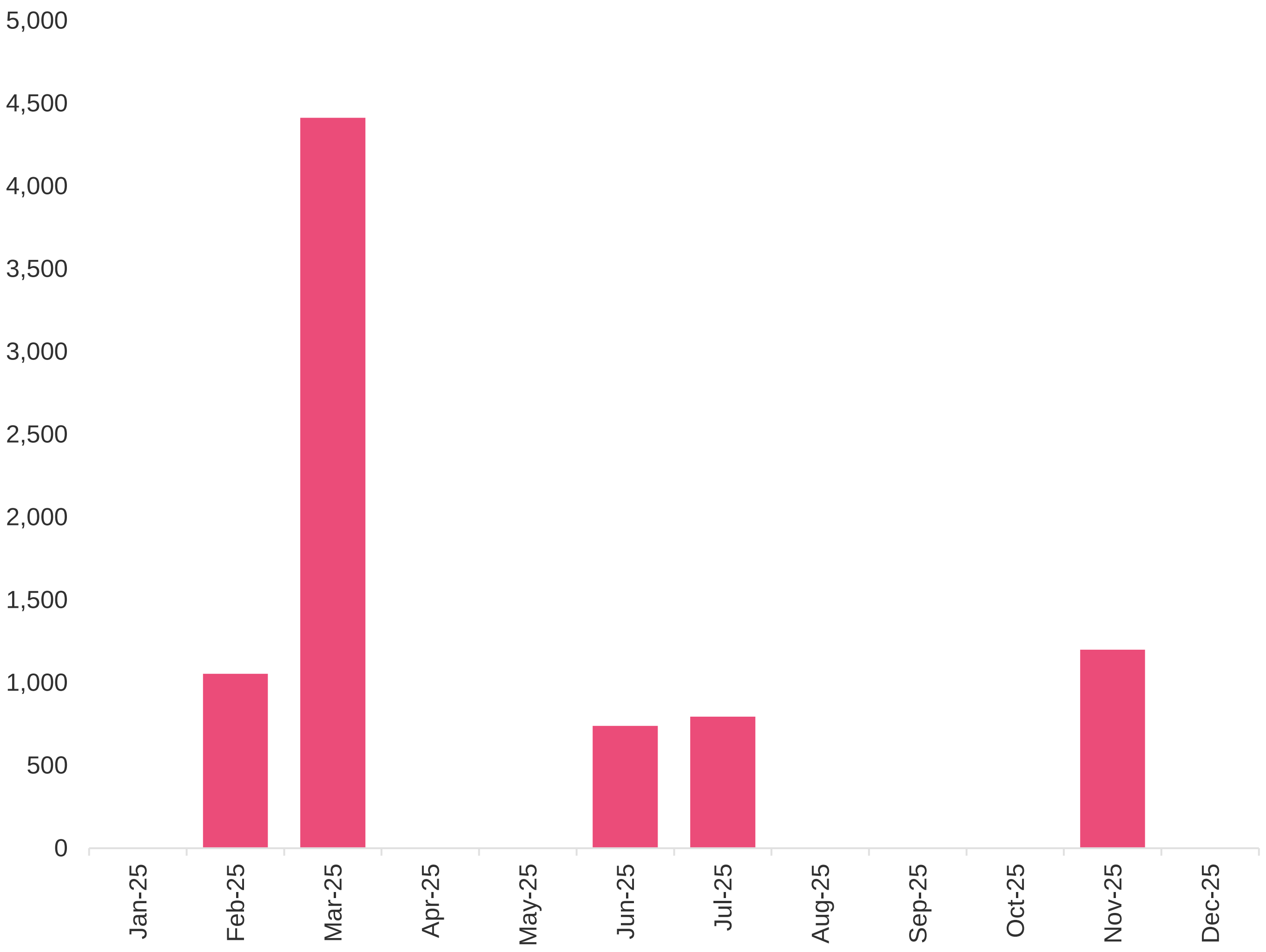
Special topic

ERSTE Group

# 2025 financing needs

**Total 2025 issuance is anticipated at approx. EUR 9.7bn**, out of which **EUR 6bn is earmarked for bonds and EUR 3.7bn to T-bills** (EUR 3.2bn maturing plus EUR 500mn net issuance target). Looking at the maturity profile, approx. **EUR 4bn goes to retail-owned maturities**, and the MoF, given the current financing strategy, is likely aiming to keep targeting retail investors, potentially adding some of the additional net issuance target. **Eurobonds in the region around EUR 2bn seems a reasonable baseline**, and with EUR 1.5bn maturing in early March, the MoF is likely to tap the market early in 2025. The remainder (approx. EUR 3.2bn) of the issuance should be targeted at the local investor base – EUR 1bn goes to short-dated papers (if retail demand were to fade, the strong bid-to-cover suggests more appetite from institutional clients). Additional issuance is more likely to target the mid-to-long end, with EUR 663mn (previously HRK 5bn) maturing in March and EUR 796mn (previously HRK 6bn) in July suggesting either one bigger issue or two smaller ones to meet the approx. EUR 2bn gap remaining. 1Q25 should bring the most issuance action, as maturities in late February / March reach EUR 5.5bn (assuming EUR 0.4bn in 3M issuance in Dec-24). **Additional Eurobond issuance remains on the table in case demand from retail investors fades throughout 2025.**

## 2025 maturity profile




Source: Eurostat, Refinitiv, Erste Group Research

# Croatia : Forecasts

| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024f | 2025f | 2026f |
|---|---|---|---|---|---|---|---|---|---|
| **Percent** | | | | | **Annual average** | | | | |
| Real GDP growth | 2.9 | 3.1 | -8.3 | 12.6 | 7.3 | 3.3 | 3.5 | 2.9 | 2.8 |
| Private consumption growth | 3.3 | 4.0 | -5.2 | 10.9 | 6.9 | 3.2 | 5.5 | 3.7 | 3.0 |
| Fixed capital formation growth | 4.4 | 12.8 | -6.3 | 4.8 | 10.4 | 10.1 | 8.8 | 3.4 | 4.0 |
| Inflation | 1.5 | 0.8 | 0.1 | 2.6 | 10.8 | 8.1 | 2.9 | 2.7 | 2.5 |
| Unemployment rate | 8.4 | 6.6 | 7.5 | 7.6 | 7.0 | 6.1 | 5.2 | 4.8 | 4.6 |
| **Percent of GDP** | | | | | | | | | |
| Budget balance | -0.1 | 0.2 | -7.2 | -2.6 | 0.1 | -0.9 | -2.2 | -2.5 | -2.2 |
| Public debt | 72.8 | 70.9 | 86.5 | 78.2 | 68.5 | 61.8 | 58.2 | 57.5 | 56.8 |
| Current account balance | 1.1 | 2.5 | -1.3 | 0.5 | -3.5 | 0.4 | -0.2 | -0.8 | -1.0 |
| | | | | | **End of year** | | | | |
| 10Y Yield | 2.04 | 0.62 | 0.66 | 0.56 | 3.77 | 3.17 | 2.90 | 2.80 | 2.90 |
| Spreads vs. German Bunds (bps) | | | | | | | 85 | 80 | 80 |



Source: Eurostat, Refinitiv, Erste Group Research

December 13, 2024

# Croatia: Country overview

**Official EU language: Croatian**

**Capital: Zagreb**

**Geographical size: 56 594km2**

**Population: 3 851 ths**

**GDP per capita: EUR 20 270, below the EU average**

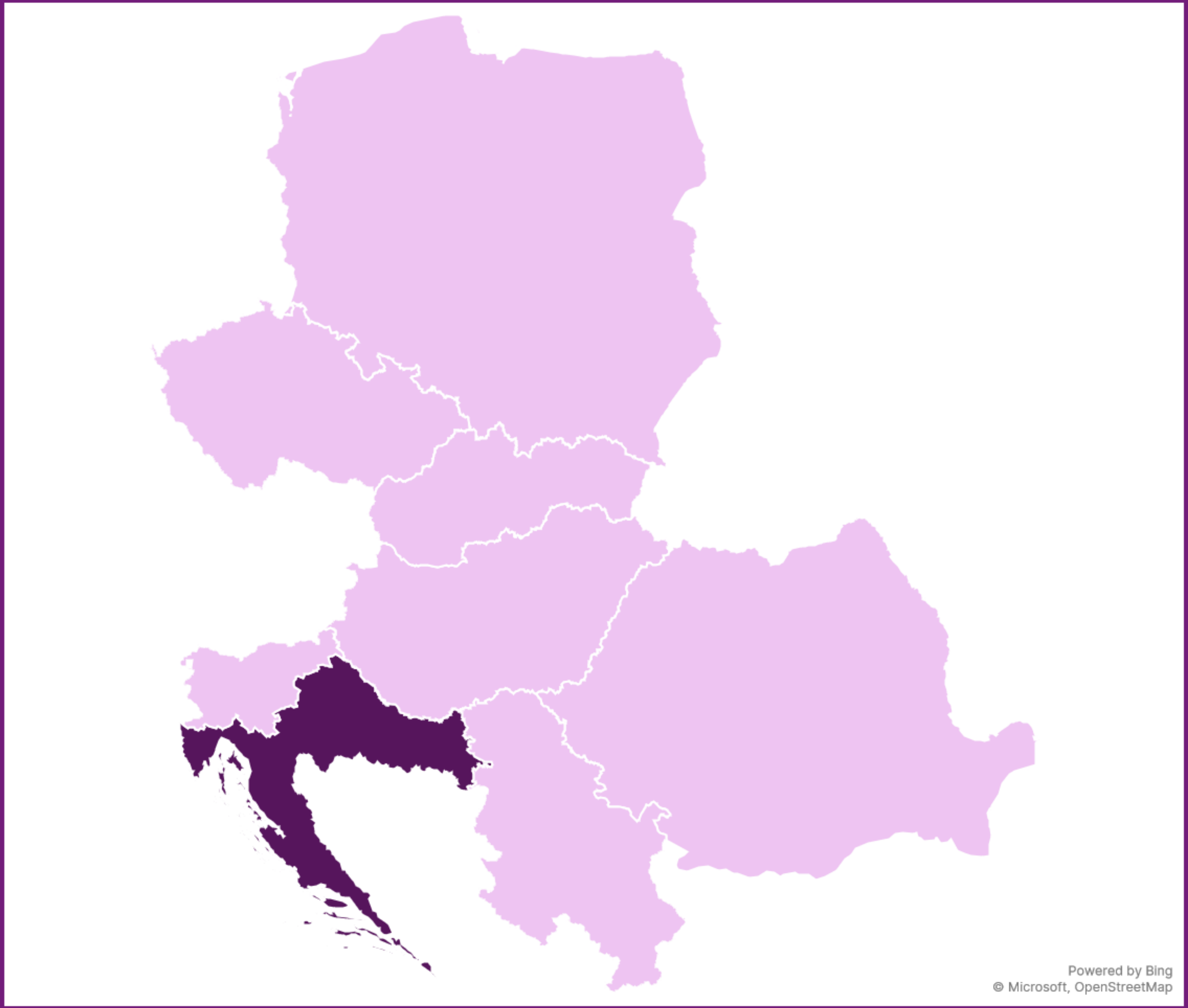
**Currency: Euro EUR since January 2023**

**Credit Ratings:**

- **Moody's: A3, outlook stable**
- **S&P: A-, outlook positive**
- **Fitch: A-, outlook stable**

**EU member state: since July 1, 2013**

**Schengen: member since January 1, 2023**






Source: Eurostat, Refinitiv, Erste Group Research
December 13, 2024

# Follow #ErsteGroupResearch on LinkedIn

Alen Kovac

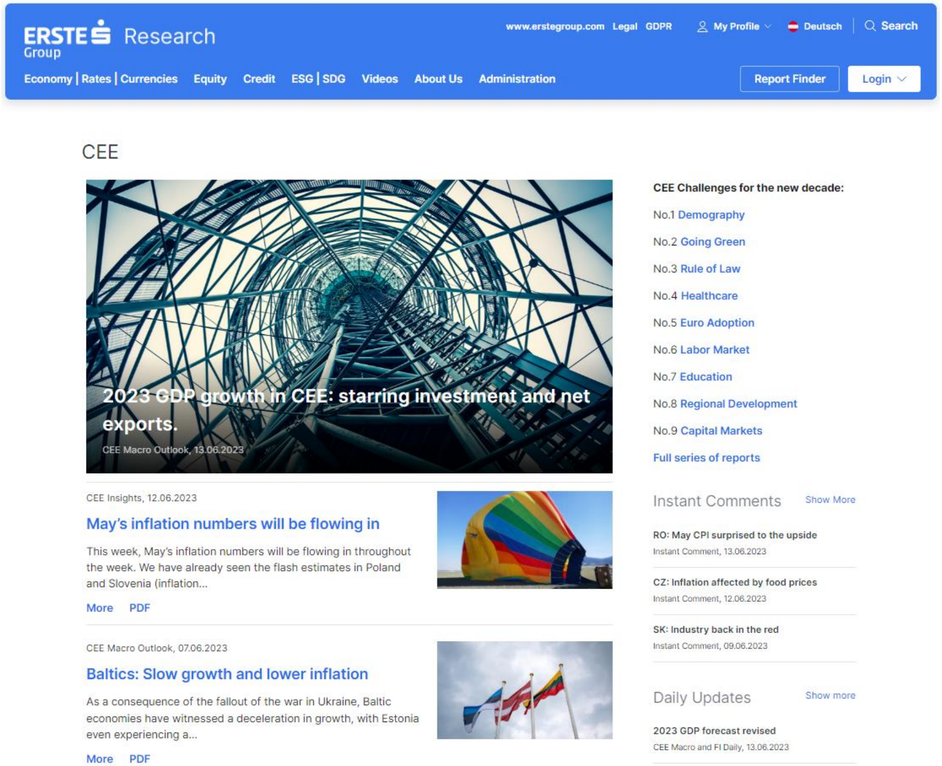
Ivana Rogic

Mate Jelic

**Give us feedback!**

# Macro reports & forecasts are publicly available on Erste Group‘s website and our mobile applications

Open in your **browser**




On your **mobile**


**Scan** our QR code

Visit our research page:
**erstegroup.com/en/research**

ERSTE Group

Source: Refinitiv, Eurostat, Erste Group Research
December 13, 2024

# Contacts

**Visit www.erstegroup.com or type on Bloomberg ESTE <GO>**

## Erste Group Research (Vienna)

**Fritz Mostböck, CEFA®, CESGA®**
**Head of Group Research**
+43 5 0100 11902
friedrich.mostboeck@erstegroup.com

**Juraj Kotian**
**Head of CEE Macro/ FI Research**
+43 5 0100 17357
juraj.kotian@erstegroup.com

**Henning Eßkuchen**
**Head of CEE Equity Research**
+43 5 0100 19634
henning.esskuchen@erstegroup.com

**Rainer Singer, CEFA®**
**Head of Major Markets & Credit Research**
+43 5 0100 11909
rainer.singer@erstegroup.com

## Local Research Offices

**Bratislava**
**Slovenska Sporitelna**
**Head: Maria Valachyova**
+421 (2) 4862 4158
valachyova.maria@slsp.sk

**Budapest**
**Erste Bank Hungary**
**Head: Jozsef Miro**
+36 (1) 235 5131
Jozsef.Miro@erstebroker.hu

**Bucharest**
**Banca Comerciala Romana (BCR)**
**Head: Ciprian Dascalu**
+40 3735 10 424
ciprian.dascalu@bcr.ro

**Prague**
**Ceska Sporitelna**
**Head: David Navratil**
+420 224 995 439
DNavratil@csas.cz

**Warsaw**
**Erste Securities Polska**
**Head: Cezary Bernatek**
+48 22 257 5751
Cezary.Bernatek@erstegroup.com

**Zagreb/ Belgrade**
**Erste Bank**
**Heads: Alen Kovac, Mladen Dodig**
+385 72 37 1383, +381 1122 09178
akovac2@erstebank.com
Mladen.Dodig@erstebank.rs

# Disclaimer

This publication was prepared by Erste Group Bank AG or any of its consolidated subsidiaries (together with consolidated subsidiaries "Erste Group") independently and objectively as general information. This publication serves interested investors as additional source of information and provides general information, information about product features or macroeconomic information without emphasizing product selling marketing statements. This publication does not constitute a marketing communication pursuant to Art. 36 (2) delegated Regulation (EU) 2017/565 as no direct buying incentives were included in this publication, which is of information character. This publication provides only other information without making any comment, value judgement or suggestion on its relevance to decisions which an investor may make and is therefore also no recommendation. Thus this publication does not constitute investment research pursuant to Art. 36 (1) delegated Regulation (EU) 2017/565. It has not been prepared in accordance with legal requirements designed to promote the independence of investment research and it is not subject to the prohibition on dealing ahead of the dissemination of investment research. The information only serves as non-binding and additional information and is based on the level of knowledge of the person in charge of drawing up the information on the respective date of its preparation. The content of the publication can be changed at any time without notice. This publication does not constitute or form part of, and should not be construed as, an offer, recommendation or invitation for a transaction in any financial instrument or connected financial instruments, and neither this publication nor anything contained herein shall form the basis of or be relied on in connection with or act as an inducement to enter into any contract or inclusion of a financial or connected financial instrument in a trading strategy. Information provided in this publication is based on publicly available sources which Erste Group considers as reliable, however, without verifying any such information by independent third persons. While all reasonable care has been taken to ensure that the facts stated herein are accurate and that the forecasts, opinions and expectations contained herein are fair and reasonable, Erste Group (including its representatives and employees) neither expressly nor tacitly makes any guarantee as to or assumes any liability for the up-to-dateness, completeness and correctness of the content of this publication. Erste Group may provide hyperlinks to websites of entities mentioned in this document, however the inclusion of a link does not imply that Erste Group endorses, recommends or approves any material on the linked page or accessible from it. Neither a company of Erste Group nor any of its respective managing directors, supervisory board members, executive board members, directors, officers of other employees shall be in any way liable for any costs, losses or damages (including subsequent damages, indirect damages and loss of profit) howsoever arising from the use of or reliance on this publication. Any opinion, estimate or projection expressed in this publication reflects the current judgment of the author(s) on the date of publication of this document and does not necessarily reflect the opinions of Erste Group. They are subject to change without prior notice. Erste Group has no obligation to update, modify or amend this publication or to otherwise notify a reader thereof in the event that any matter stated herein, or any opinion, projection, forecast or estimate set forth herein, changes or subsequently becomes inaccurate. The past performance of a financial or connected financial instrument is not indicative for future results. No assurance can be given that any financial instrument or connected financial instrument or issuer described herein would yield favorable investment results or that particular price levels may be reached. Forecasts in this publication are based on assumptions which are supported by objective data. However, the used forecasts are not indicative for future performance of financial instruments incl. connected financial instruments. Erste Group, principals or employees may have a long or short position or may transact in financial instrument(s) incl. connected financial instruments referred to herein or may trade in such financial instruments with other customers on a principal basis. Erste Group may act as a market maker in financial instruments, connected financial instruments or companies resp. issuers discussed herein and may also perform or seek to perform investment services for those companies resp. issuers. Erste Group may act upon or use the information or conclusion contained in this publication before it is distributed to other persons. This publication is subject to the copyright of Erste Group and may not be copied, distributed or partially or in total provided or transmitted to unauthorized recipients. By accepting this publication, a recipient hereof agrees to be bound by the foregoing restrictions.

Erste Group is not registered or certified as a credit agency in accordance with Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies (the Credit Rating Agencies Regulation). Any assessment of the issuers creditworthiness does not represent a credit rating pursuant to the Credit Rating Agencies Regulation. Interpretations and analysis of the current or future development of credit ratings are based upon existing credit rating documents only and shall not be considered as a credit rating itself.



Published by:
Erste Group Bank AG
Group Research
1100 Vienna, Austria, Am Belvedere 1
Head Office: Wien
Commercial Register No: FN 33209m
Commercial Court of Vienna

Erste Group Homepage: www.erstegroup.com