

# Croatia

By Leonardo Mancini, European Mortgage Federation – European Covered Bond Council

## IN A NUTSHELL

- There was an economic recovery with GDP growing by 10.2%, unemployment at 7.6%, inflation rising to 2.7% and a rating upgrade.
- House prices rose by 7.3%.
- Number of permits increased by 7.3%.
- A government-subsidised housing loans programme, which has been extended until 2023 has already helped 4,559 people (out of 4,739 applications) buy houses, The programme is targeted at younger buyers, with an average age of 32 years and loan amount of EUR 75,000.
- Croatia introduced a Reconstruction of Building initiative and drafted a Long-term Strategy for National Building Stock Renovation to increase the rate of renovation and reconstruction of the building stock.

## MACROECONOMIC OVERVIEW

In December 2020, Fitch upgraded Croatia's Long-Term Foreign-Currency Rating to an all time high of BBB, with Positive Outlook. Standard & Poor's credit rating of BBB- with stable outlook remains and Moody's rates Croatia is Ba2 with positive outlook. The rating agencies claim that adoption of the euro will benefit Croatia's credit profile.

After contracting by 8% in 2020, the economy recovered by 10.2% in 2021, almost twice the European Union average of 5.4%, reaching a GDP level of ca EUR 57.2 bn. The main contributor to this was exports of goods and services. The unemployment rate increased slightly to 7.6% in 2021 from 7.5% in 2020.

In July 2020 Croatia joined the Exchange Rate Mechanism and the Croatian National Bank (CNB) established a close cooperation framework with the European Central Bank. In light of this, the central rate of the Croatian kuna was set at 7.5345 HRK per 1 EUR with a standard fluctuation band of  $\pm 15\%$ .

Government debt decreased from 81.3% of GDP in 2020 to 79.8% in 2021, returning to the downward trend in. In 2021 the currency (HRK) registered an average annual exchange rate of about 7.5284 HRK per 1 EUR.

The average annual inflation rate increased from 0.0% in 2020 to 2.7% in 2021, breaking the relatively stable period since 2017, and reaching the highest level since 2013. The Croatian government put forward a set of new fiscal measures to contain the effects of the pandemic, amounting to almost 8% GDP. These measures included employment subsidies and shortened working hours schemes. Additionally, the national government drafted the 'National Recovery and Resilience Plan' (NRRP) from 2021 to 2023, which consists of 146 investments and 76 reforms endowed with EUR 6.3 bn worth of grants. This plan covers different areas such as public administration, justice and state assets;

education, science and research; labour market and social protection; health etc., focusing mainly on the green and digital transitions.

## HOUSING MARKETS

The average price per square meter in 2020 was HRK 13,713 (ca EUR 1,821), an increase of 7.8% from 2020. The calculation includes prices of new dwellings in the private market (HRK 13,843, ca EUR 1,838), as well as those constructed under the government "Publicly Subsidised Residential Construction Program" (HRK 7,642 on average, ca EUR 1,015).

In Zagreb, the average price of new dwellings per square meter was HRK 14,672 (ca EUR 1,950), around 4.7% more than 2020.

The nominal house price index (which considers new and existing dwellings together) increased by 7.3%, slightly more than Zagreb's nominal house price index, which increased by 7.2%. Whereas the Adriatic coast residential dwelling prices grew at a faster rate of 8.2%. It is important to highlight that the increasing trend for all urban areas in Croatia has been on going since 2015.

Despite the decrease in 2020, the number of building permits issued was 16.654 in 2021, a 7.3% increase. The expected value of works linked to these permits increased by 13.6% after a decrease of 2020. By types of constructions, 85.2% of permits were issued for buildings and 14.8% for civil engineering works. By types of works, 76.9% of permits were issued for new constructions and 23.1% for reconstruction.

## MORTGAGE MARKETS

### MARKET DYNAMICS

The Croatian National Bank (CNB) in 2021 adopted a macroprudential policy to maintain capital levels and increase resistance to possible losses by temporarily limiting dividend distribution.

Bank assets (of which 90.6% are owned by foreign shareholders) accounted for 99.0% of the total assets of credit institutions, which increased in 2021 to a record high value of HRK 500.8 bn (ca EUR 66.5 bn) due to an increase in household and corporate deposits. Due to pandemic related uncertainty credit institutions were more risk averse resulting in an increase in liquid assets qualifying for Liquidity Coverage Ratio which rose to an aggregate 202.5%, over 20% more than in 2020. The total capital ratio of all credit institutions averaged 25.6%. The share of housing savings banks' assets continued to decrease and amounted to the remaining 1.0%.

The growth of optimism and favourable financial conditions, supported by an expansive monetary policy, facilitated the lending activity of banks, primarily in the retail segment. Loans to households grew the most: from 2.1% at the

end of 2020 to 4.5% at the end of 2021.

Interest rates on new loans to companies and households mostly continued to fall during 2021. New loans to companies were at an all time low average of 1.3%. But the average interest rate on new retail loans increased from 3.6% at the end of 2020 to 3.9% at the end of 2021, mainly due to the financing structure of this sector, which was helped by the subsidy program.

The NPL ratio which continued to improve to 4.3% from 7.1% in 2020, although still worse than the EU average. NPLs decreased for non-financial companies and households and sales of some non-performing loans also helped the ratio improvement.

### NON-MARKET LED INITIATIVES

Over the last four years, two major legislative changes have influenced the mortgage market. First, the introduction of the Subsidised Housing Loans Act, and second, the reduction in real estate transfer tax.

In 2017, the Government introduced the subsidised housing loan programme, for which Croatian citizens under 45 years old may get a subsidy to buy a house up to a maximum of EUR 1,500 per square meter or a total of EUR 100,000 (equivalent). The loan repayment period must be at least 15 years. This is to support the regeneration and reconstruction of society, by incentivising young people not to leave the country. In 2021 4,599 out of 4,739 applications were approved. The average loan under the scheme was for EUR 75,000 and the average borrower 35 years old. The scheme will continue until 31 December 2023.

In 2019, the real estate transfer tax was reduced from 4% to 3%. This is a second reduction in recent years, it was cut from 5% in 2017.

### MORTGAGE FUNDING

According to the Croatian National Bank Annual Report for 2021, retail deposits grew. Due to low interest rates, deposits are undergoing a structural change: shifting from term to on demand deposits. A covered bond law was introduced for the first time in April 2022.

### GREEN FUNDING

Amongst the initiatives of the National Recovery and Resilience Plan, Croatia has undertaken the Reconstruction of Building initiative, to contribute to the wave of building reconstruction with energy-efficient and decarbonised building stock. This was boosted by the earthquake in 2020 which caused considerable damage; EUR 600 mn out of the total of EUR allocated to building renovation, are for earthquake damaged buildings including their energy renovation. In addition to them, other EUR 134 mn are allocated to energy renovation of buildings not affected by earthquakes.

In the period leading up to 2030, the aim is to increase the rate of renovation to 3%, and to this end the Long-term Strategy for National Building Stock Renovation by 2050 was drafted. Renovation programmes have been envisaged in the Integrated National Energy and Climate Plan for the period 2021 – 2030. on the use of buildings. Many energy renovation projects were implemented in the period 2014-2020, and the recorded rate of renovation of the building stock was 0.7% or 1.35 mn m<sup>2</sup>/year.

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To achieve the strategic goals of reducing energy consumption in buildings, three key energy programs are foreseen for the 2021-2030 period targeting apartment buildings, family houses and public buildings.

|  | CROATIA<br>2020 | CROATIA<br>2021 | EU 27<br>2021 |
|--|-----------------|-----------------|---------------|
| <b>MACROECONOMIC VARIABLES</b>                                   |                 |                 |               |
| Real GDP growth (%) (1)  | -8.1            | 10.2            | 5.4           |
| Unemployment Rate (LSF), annual average (%) (1)                  | 7.5             | 7.6             | 7.0           |
| HICP inflation (%) (1)   | 0.0             | 2.7             | 3.0           |
| <b>HOUSING MARKET</b>  |                 |                 |               |
| Owner occupation rate (%) (1)                                    | 91.3            | 90.5            | 70.0          |
| Gross Fixed Investment in Housing (annual change)(1)             | n/a             | n/a             | 6.6           |
| Building Permits (2015=100) (2)                                  | 202.6           | 239.6           | 134.0         |
| House Price Index – country (2015=100) (2)                       | 130.4           | 139.9           | 145.2*        |
| House Price Index – capital (2015=100) (2)                       | 142.5           | 152.7           | 146.1*        |
| Nominal house price growth (%) (2)                               | 7.7             | 7.3             | 10.3*         |
| <b>MORTGAGE MARKET</b>   |                 |                 |               |
| Outstanding Residential Loans (mn EUR) (2)                       | 8,233           | 9,016           | 6,508,621     |
| Outstanding Residential Loans per capita over 18 (EUR) (2)       | 2,450           | 2,696           | 17,782        |
| Outstanding Residential Loans to disposable income ratio (%) (2) | n/a             | n/a             | 62.8*         |
| Gross residential lending, annual growth (%) (2)                 | 37.3            | 0.3             | 12.2          |
| Typical mortgage rate, annual average (%) (2)                    | 2.9             | 2.7             | 2.0           |

\* Please note that this value is the simple average of the available values in 2021.

#### Sources:

(1) Eurostat

(2) European Mortgage Federation - Hypostat 2022, Statistical Tables.

## CROATIA FACT TABLE

|   |   |
|---|---|
| <b>Which entities can issue mortgage loans in your country?</b>   | Commercial banks and housing saving banks.  |
| <b>What is the market share of new mortgage issuances between these entities?</b>                                     | Commercial banks dominate the market.   |
| <b>Which entities hold what proportion of outstanding mortgage loans in your country?</b>                             | Commercial banks hold approximately 94.5%, and housing saving banks hold the rest 5.5%.   |
| <b>What is the typical LTV ratio on residential mortgage loans in your country?</b>                                   | Between 70 and 80%, even though there is been a substantial share of new loans had a loan-to-value (LTV) ratio higher than 90 % in the first half of 2021.  |
| <b>How is the distinction made between loans for residential and non-residential purposes in your country?</b>        | <p>The 'Consumer Housing Loans Act' defines "housing loan" as a loan: a) collateralised by a security on residential immovable property or a transfer of ownership of residential immovable property for the purpose of securing the loan; or b) the loan the purpose of which is for the consumer to acquire or retain the ownership of residential immovable property.</p> <p>Loans not falling within this description would not be residential.</p> |
| <b>What is/are the most common mortgage product(s) in your country?</b>   | Housing and mortgage loans.   |
| <b>What is the typical/average maturity for a mortgage in your country?</b>   | Between 20 and 30 years.  |
| <b>What is/are the most common ways to fund mortgage lending in your country?</b>                                     | Deposits.   |
| <b>What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?</b> | Real estate transfer tax (3% of market value); transaction costs (fees and commissions): up to 2% of market value; and other costs (agency intermediation, public notary, etc.): 2-4% of market value.  |
| <b>What is the level (if any) of government subsidies for house purchases in your country?</b>                        | Low (in the part of government supported "Publicly Subsidised Residential Construction Programme", through the governmental incentives for housing savings and through the limited government financial support for first housing property purchase).   |