Croatia

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IN A NUTSHELL

- → Croatia joined the Euro and the Schengen area on 1st January 2023.
- → Economic growth slowed to 3.1%, is expected to remain broadly similar in the medium term.
- → Inflation slowed but is still above the Eurozone average due in particular to wage increases.
- → House prices continue to rise, as does the rate of construction of new housing.

MACROECONOMIC OVERVIEW

Croatia became the 20th country in the Eurozone on 1st January.

Economic growth slowed to 3.1% from 7% in the previous year (and 13% in 2021), still substantially above the rate of growth in the Eurozone economy as a whole (0.4%) and continuing an 8-year run of growth in excess of 2.5% (with the exception of the pandemic year). The main drivers of this growth were exports, household and government consumption and investment, which was underpinned by drawdowns under EU funds, specifically the Multiannual Financial Framework (MFF) and the Recovery and Resilience Facility (RRF).

Given this growth, the labour market remains tight with employment growing by 2.7% leaving unemployment constant at 6.2% – the discrepancy being due to an enlarged workforce, mainly due to an influx of workers from non-EU countries – and income in real terms grew by 2.0% (+5.7% in 2022), substantially above the eurozone (which shrank by 2.2% in 2023, after 0.6% growth in 2022). Reflecting this growth, inflation (HCIP) was 8.5% (from 10.7% in 2022), still significantly above that in the rest of the Eurozone (5.4%). Prices of services were the largest component of this growth, partly offset by reduced energy price inflation, which in turn was partly due to government subsidy measures.

The government fiscal deficit was 0.7% of GDP which, combined with the economic growth reduced the debt: GDP ratio to 63%, it is expected to fall to below the Growth and Stability pact target of 60% during 2024. The three main rating agencies all revised their outlook for the country's rating to 'positive' from 'stable', it is now BBB+ from S&P and Fitch and Baa2 from Moody's.

LOOKING AHEAD

According to European Commission forecasts, growth is expected to continue at a similar level although the main drivers will increasingly be household consumption, exports of goods and tourism. Investment activity is expected to slow with the completion of the MFF and the expiry of the EU Solidarity Fund (for reconstruction after the 2020 earthquake) before increasing again from 2025, although Commission has highlighted a risk that the uptake of funds could be limited by capacity constraints. Lower Eurozone interest rates and increased credit availability should also contribute to growth.

The labour market is expected to remain tight with a decrease in unemployment to 5.6% by the end of 2025 and increasing pressure on wages. Wage rises in particular in the service sector will moderate the fall in inflation – prices for services are predicted to continue to increase – but overall inflation is expected to continue to decline, to 3.5% in 2023 and 2.2% in 2025.

The government deficit is expected to increase as a result of public sector wage inflation, social assistance measures and reduced tax rates reaching 2.6% of GDP in both 2024 and 2025. This increase should be mitigated by wage increases, economic growth and increased tourism. Measures to mitigate the effect of energy price shocks will cost the government 0.6% of GDP, down from 1.9% in 2023. Overall, the debt: GDP ratio will continue to improve to a forecast 59.5% in 2024 and 59.1% in 2025.

HOUSING MARKETS

House prices continued to rise albeit at a slower rate of 9.4%, from 17% in 2022, significantly exceeding price increases in the EU as a whole (which rose by 0.1%) and the Eurozone where they fell by 1.2%. In Q4 prices actually fell slightly, before returning to growth in the first quarter of 2024.

Reflecting house price increases and lower price increases in building costs (which only increased by 4.7%), construction of residential property has increased, permits were issued for 3.6mn m^2 of new builds, and the construction sector now represents 3.5% of national GDP – both the highest values since this data was collected.

Regionally, the Adriatic coast region had the largest price increases, largely as a result of foreign purchases and favourable tax treatment for rental activity in the tourism sector. Prices in Zagreb city also rose significantly.

The percentage of Croatian's owning their own home, already the third highest in Europe (behind Romania and Slovakia) increased further to 91.2% (from 91.1%). According to Eurostat, Croatia is also characterized by the highest average age of leaving the parental home in Europe.

MORTGAGE MARKETS

Commercial banks dominate the mortgage market with nearly 95% of total outstanding loans. Housing savings banks having the residual 5%. At origination mortgages are typically for 70 to 80% of the value of the property and are for between 20 and 30 years.

Non-performing loans in the sector continued to decrease from 5.0% at the start of the year to 4.2% by year end (all loans to households).

Affordability and debt to income ratios have not deteriorated as much as in many other EU countries as the adoption of the Euro resulted in lower interest rates (which mitigated some of the increase in Euro interest rates).

MORTGAGE FUNDING

The banking market continues to be dominated by foreign owned banks which account for 90% of total banking assets and is characterised by very low loan to deposit ratios, negligible use of wholesale funding and relatively small mortgage exposure (approximately 20% of total balance sheets).

Although a covered bond law has been in place since 2022 it is as yet unused.

The healthy liquidity of banks may be threatened by further issues of retail bonds by the Ministry of Finance, in 2023 EUR 3 bn of such bonds were issued to retail investors.

GREEN FUNDING

Although several banks offer loans to their customers to enhance the energy efficiency of their homes there has not yet been a green bond issued by any banks in Croatia.

	CROATIA 2022	CROATIA 2023	EU 27 2023
MACROECONOMIC VARIABLES			
Real GDP growth (%) (1)	7.0	3.1	0.4
Unemployment Rate (LSF), annual average (%) (1)	7.0	6.1	6.1
HICP inflation (%) (1)	10.7	8.4	6.4
HOUSING MARKET			
Owner occupation rate (%) (1)	91.1	91.2	69.2
Gross Fixed Investment in Housing (annual change) (1)	n/a	n/a	-3.1
Building Permits (2015=100) (2)	269.1	142.0	94.0
House Price Index - country (2015=100) (2)	170.1	186.2	170.2*
House Price Index - capital (2015=100) (2)	193.9	0.0	165.1*
Nominal house price growth (%) (2)	17.3	9.5	3*
MORTGAGE MARKET			
Outstanding Residential Loans (mn EUR) (2)	9,932	10,840	6,782,375
Outstanding Residential Loans per capita over Total Population (EUR) (2)	2,572	2,815	15,114
Outstanding Residential Loans to disposable income ratio (%) (1) (2)	24.3	n/a	71.3
Gross residential lending, annual growth (%) (2)	67.0	1.5	-26.6
Typical mortgage rate, annual average (%) (2)	2.5	n/a	4.7

* Please note that this value is a simple average of the available values in 2023.

Sources:
(1) Eurostat.
(2) European Mortgage Federation - Hypostat 2024, Statistical Tables.

CROATIA FACT TABLE

Which entities can issue mortgage loans in your country?	Commercial banks and housing saving banks.
What is the market share of new mortgage issuances between these entities?	Commercial banks dominate the market.
Which entities hold what proportion of outstanding mortgage loans in your country?	Commercial banks hold approximately 94.5%, and housing saving banks hold the rest 5.5%.
What is the typical LTV ratio on residential mortgage loans in your country?	Between 70 and 80%.
How is the distinction made between loans for residential and non-residential purposes in your country?	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. Loans not falling within this description would not be residential.
What is/are the most common mortgage product(s) in your country?	Housing and mortgage loans.
What is the typical/ average maturity for a mortgage in your country?	Between 20 and 30 years.
What is/are the most common ways to fund mortgage lending in your country?	Deposits.
What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?	Real estate transfer tax (3% of market value, application from January 2019); transaction costs (fees and commissions): up to 2% of market value; and other costs (agency intermediation, public notary, etc.): 2-4% of market value.
What is the level (if any) of government subsidies for house purchases in your country?	Low (in the part of government supported "Publicly Subsidized Residential Construction Program", through the governmental incentives for housing savings and through the limited government financial support for first housing property purchase).