

Concluding Notes

In 2007, the macroeconomic environment was marked by a sharp increase in real GDP of the Croatian economy, positive labour market trends and a slowdown in external debt. However, the inflation rate accelerated and the current account deficit increased. The sharp acceleration of real GDP growth resulted from the accelerated growth in household disposable income and strong corporate foreign borrowing, which drove up personal consumption and kept investments at a high level. As regards the labour market, employment continued to rise and unemployment dropped further. In contrast, significant supply-side shocks led to sharp increase in consumer price inflation in 2007, especially in the second half of the year.

Against this background, the CNB continued to focus its monetary policy on ensuring the stability of the nominal exchange rate of the kuna versus the euro and enacted measures which considerably slowed down the growth of bank placements.

A stable kuna exchange rate has been the main anchor of domestic inflationary expectations and a key precondition for domestic price stability. In overall, the kuna exchange rate appreciated only to a slight extent against the euro in 2007. Appreciation pressures, persisting for most part of the year, primarily resulted from the seasonal foreign exchange inflow from tourism, foreign exchange supply generated by corporate foreign borrowing and inflow of foreign exchange aimed at bank recapitalisation. In addition, the appreciation of the kuna/euro exchange rate was also due to the growth of demand for the kuna for securities investments in the domestic market, which in 2007 registered a record high annual share turnover, twice as many transactions as in 2006 and highest value of the ZSE index, CROBEX, on record. The central bank mitigated these appreciation pressures by foreign exchange interventions and managing liquidity through reverse repo operations.

In addition to the marginal reserve requirement rate of 55% and the minimum foreign currency ratio of 32%, the CNB's Decision on the purchase of compulsory CNB bills also contributed to curbing the increase in bank placements by prescribing the purchase of CNB bills for banks whose placement growth in 2007 exceeded 12%. These central bank measures were effective in decelerating the growth of bank placements, with banks remaining oriented to household lending and adjusting to the said Decision by moderating corporate lending. However, companies responded to these conditions by making use of other financing sources, with the result that the annual growth of their total debt failed to slow down.

The external debt of the economy as a whole slightly decelerated in 2007. This was also a result of monetary policy measures, as the sharp slowdown in bank placement growth led to a high drop in banks' external debt.

The imbalance in international trade in goods worsened in 2007. In contrast, other current transactions accounts, especially the services account, improved compared with the previous year, but not to a degree sufficient to halt the current account deficit growth. The capital and financial transactions account recorded a sharp increase in net foreign direct investments in the RC, whose amount exceeded the current account deficit. International reserves of the RC continued to grow in 2007.