

PBZ Weekly Analysis

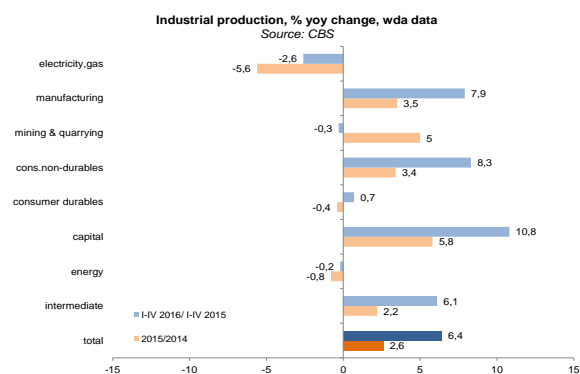
Number 519, June 06, 2016

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Weekly overview

- According to the preliminary data of the Croatian Bureau of Statistics (CBS), GDP for the first quarter of 2016 increased by 2.7% compared with the same quarter of 2015 (gross indices), while the comparison with the last three months of the previous year shows an increase of 0.6% (seasonally adjusted data). According to components, personal consumption rose by 3.1% yoy (+2.4% in 4q15), due to an increase in the real household income and positive changes in the labour market, while government spending increased by 0.6%. A substantial growth of 4.3% was recorded by investments as well (possibly spurred by a better absorption of EU funds) and, consequently, the contribution of total domestic demand to the GDP growth amounted to 2.8 percentage points. Although the largest individual positive contribution was realised by the exports of goods and services (which were up in real terms by 7.1%), a simultaneous rise in imports (of 6.1%) resulted in total negative contribution of net external demand to the GDP growth. Positive movements continued over the second quarter and, according to the CBS data, April saw an increase in the industrial production of 4.9% and real retail trade of 3.2%.

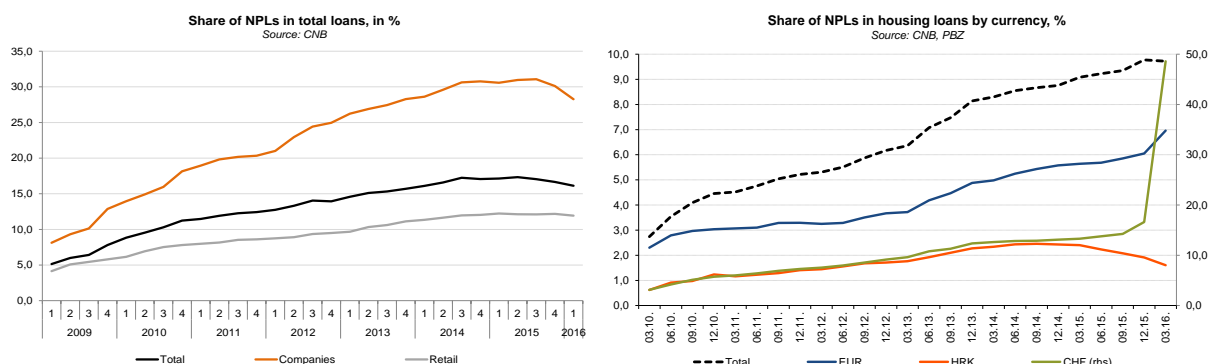
- The industrial production in April 2016 rose by 4.9% yoy (wda data), whereas mom data show a decrease of 2.9% (seasonally and working-day adjusted data). According to MIGs, the yoy production of Intermediate and Capital goods was up by 8.2% and 5.1%, respectively, as a result of larger external demand, while the growth of



- 6.7% recorded in Consumer non-durables is related to the recovery of domestic demand. IP for Consumer durables rose by 0.6%, while Energy production declined by 3.2%. According to NKD, Manufacturing (with almost a 78% share in total production) increased by 7.3% yoy (of which production of food +10.9%), Mining and quarrying was up by 3.3%, while Electricity, gas, steam and air conditioning supply was down by 7.1%. The cumulative data for the first four months show an increase in the industrial production of 6.4% yoy.

- Positive trends in loan quality have continued for the third consecutive quarter and, after a fall of 0.5 p.p. qoq recorded in the third and fourth quarter of 2015, the first quarter this year saw a decrease in the share of non-performing loans in total loans of 0.5 p.p. to 16.1%. The described movements are primarily a result of a substantial fall related to loans to non-financial corporations (-1.9 p.p.), while for loans to households the rate of decrease was more moderate (-0.3 p.p.). Thus, the share in the corporate sector dropped to 28.3%, while in households to 11.9%. As we have explained earlier, a decrease in the portfolio of non-performing loans is a result of stronger activities related to their sale, or balance sheet cleaning, by which banks set out conditions to ensure a basis for a stable business in the upcoming period. According to purpose, all types of loans to households have recorded a

decline in the share qoq. The strongest fall was recorded by loans for other purposes (-1.1 p.p. to 33.3%), followed by any-purpose cash loans (-0.6 p.p. to 8.6%), while overdrafts declined to 0.2 p.p. to 12.1%. Undoubtedly, the most interesting movements were recorded in housing loans, where the share was reduced by 0.1 p.p. to 9.7%, while the share of loans indexed to the euro was around 7.0% and loans indexed to the kuna around 8.0%, on the other hand, the share of loans indexed to the franc surged to 48.6%. The latter high figure is somewhat misleading as it is a result of the conversion and the consequential reduction in the total portfolio volume with predominating NPLs, however, the total amount of NPLs indexed to the franc has in fact been reduced in half. The total coverage of partly recoverable and totally irrecoverable loans with value adjustment costs continued its growth trend, reaching 58.4%. The coverage of corporate loans has slowly approached the coverage for household loans, amounting to 56.7% by the end of March (+1.5% p.p. qoq). The ratio for household loans climbed to 61.5% (+1.9% p.p.) and is therefore still under the levels recorded in the pre-crisis 2007 (67.0%).

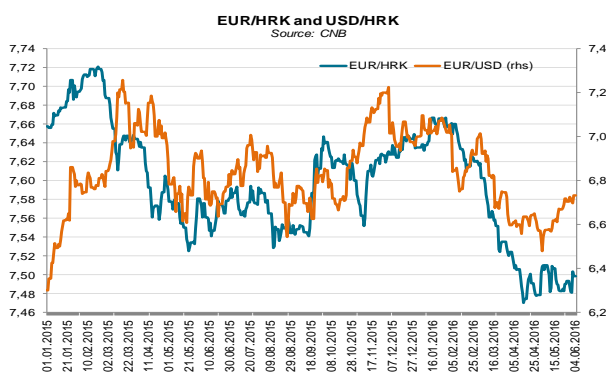
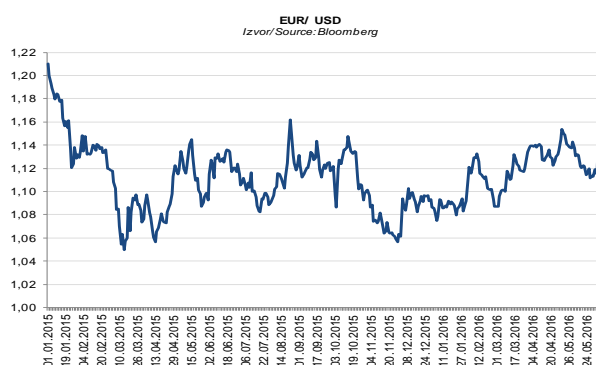


- After hitting the historic low levels last year, due to losses caused by the conversion, the profitability of credit institutions has been recovering this year. Over the first quarter, net interest income amounted to 2.7 billion kuna, up by 0.7% yoy, while net fee income rose by 3.9% to 0.8 billion kuna. However, as other income was negative due to realised losses under loans and receivables amounting to 0.3 billion kuna (conversion), gross operating profit dropped by 6.3% yoy, amounting to 3.4 billion kuna. Operating costs increased by 3.1% to 2.1 billion kuna, owing to a significant rise in the deposit insurance premium, i.e. contributions to the Single Resolution Fund, which resulted in the fall in net operating income by 18.7% to 1.3 billion kuna and a consequential rise in the cost to operating income ratio to 62.5% (1Q 2015: 56.8%). Regardless of the lower net operating profit, credit institutions recorded a 2.5 times higher gross profit, due to income from value adjustments and provisions amounting to 0.25 billion kuna (0.15 billion kuna from reversal of provisions under housing loans). Net profit of credit institutions reached 1.2 billion kuna in the first quarter, up by 145.0% yoy. According to the preliminary data, the ten largest banks recorded business profit in the first quarter, while the number of banks which recorded business losses was reduced to six, with a market share lower than 1%. The total capital ratio of banks at the end of March amounted to a still high 21.8%, or a total of 21.9% for credit institutions.

CNB intervenes

As expected, at its last week's meeting, the ECB decided to maintain interest rates at the current levels, however the trend of the strengthening of the dollar against the euro suddenly reversed at the end of the week, following the release of the disappointing data from the U.S. labour market. The latter has dispelled expectations that the Fed will raise interest rates this month, but also the anticipations that the interest rate hike will occur in July have been significantly lessened. The trading on Friday closed at 1.1367 dollar to the euro, up by 2.3% wow.

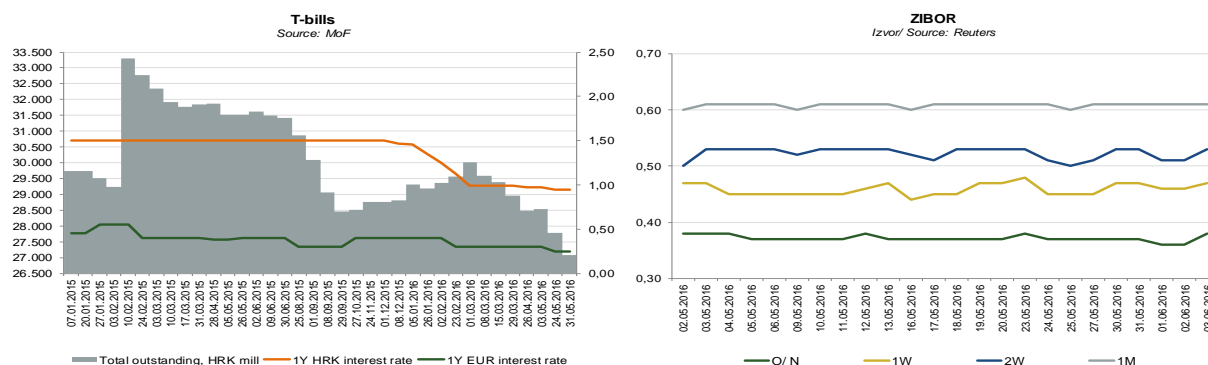
Last Tuesday, after a decrease in the EUR/HRK exchange rate towards 7.475-7.48, the central bank intervened at the market to prevent a stronger domestic currency appreciation. A total of 83.5 million euro was purchased from the banks at the average exchange rate of 7.4925 kuna to the euro. Thus, the pressures were reduced and the mid-exchange rate on Friday amounted to 7.4982, up by 0.1% wow, while the kuna against the dollar weakened by 0.4% to 6.7308 kuna to the dollar. After a more active last week, we anticipate a slightly lower trading this week, ranging from 7.48-7.51.



Money market calm

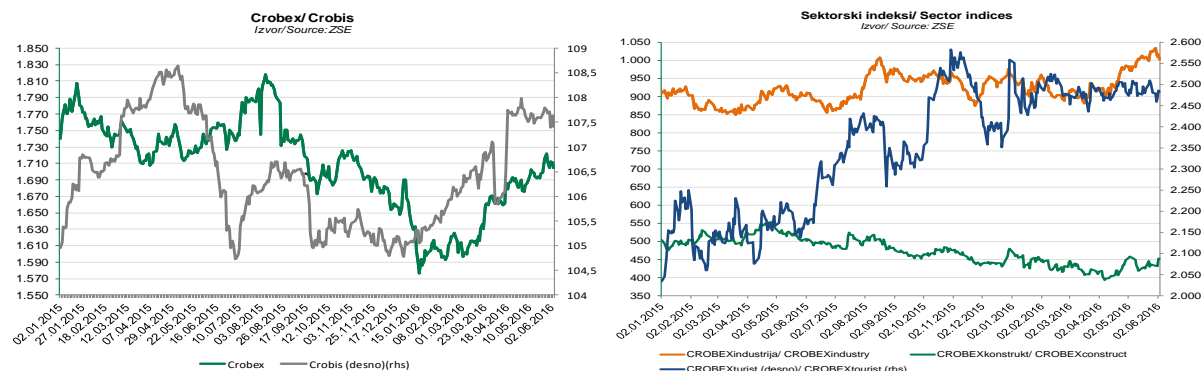
The money market has continued to record ample liquidity with weak demand and low trading volumes. A total of 80 million kuna at the fixed repo rate of 0.50% were injected in the system at the regular reverse repo auction again, whereas the total ZMM turnover amounted only to 5 million kuna, where supply exceeded demand by an average of 332 million kuna per day. The overnight Zibor closed the week at a 1 b.p. higher level of 0.38%, while 1M and 3M remained at 0.61 and 0.80%, respectively.

The MF auction saw a subscription of 683 million kuna and, as 1.4 billion kuna matured, the government debt under T-bills dropped to 27.1 billion kuna. There was a subscription of 683 million kuna in one year kuna T-bills with an unchanged interest rate of 0.95%. This week, a total of 0.8 billion kuna will mature and the auction with the planned issue of 600 million kuna has been announced.



Crobex drops wow

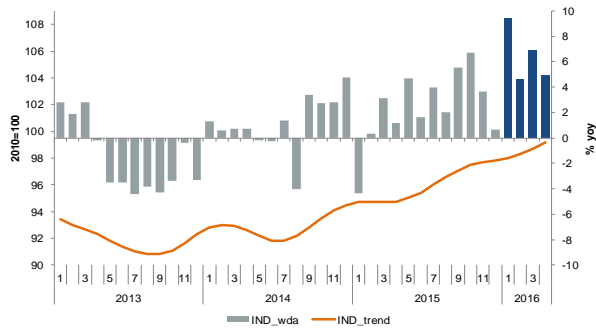
The Crobex index dropped by 1.0% wow, closing the week at 1,704.14 points, whereas the Crobis declined by 0.3% wow, closing the week at 107.41 points. With regard to sector indices, CROBEXconstruct increased by 4.0% wow (to 452.57 points), CROBEXtourist moderately rose by 0.1% (to 2,482.97 points), while CROBEXindustry decreased by 2.0% wow (to 1,003.18 points). Last week, a day longer, the total ZSE turnover rose 2.5 times from the week before (to 1.1 billion kuna), due to a multiple increase in the turnover in shares (to 400.4 million kuna, where the sale of 526,926 state-owned shares of the company Končar to pension funds amounted to 360 million kuna) and a 1.7 times higher turnover in bonds (to 659.9 million kuna).



Statistics

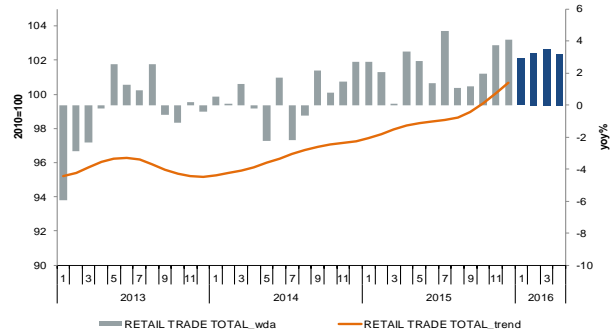
Industrial production, wda yoy % ch.

Source: Eurostat



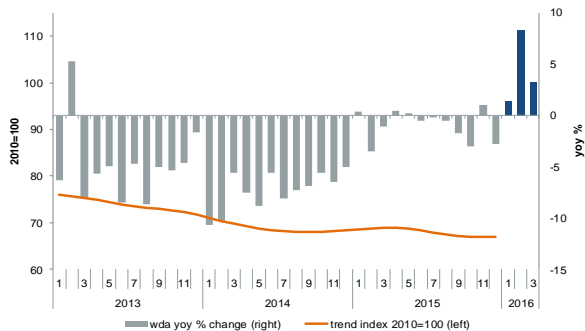
Retail trade, real, wda yoy ch.

Source: CBS



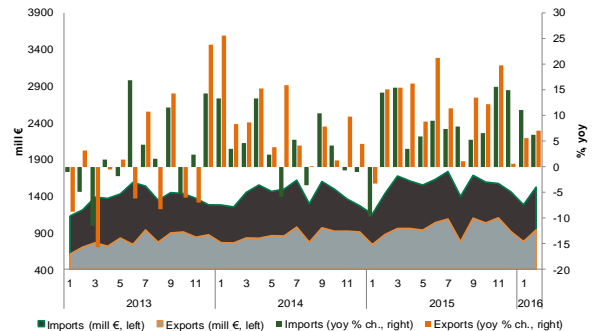
Construction works, yoy % ch. and index 2010=100

Source: CBS



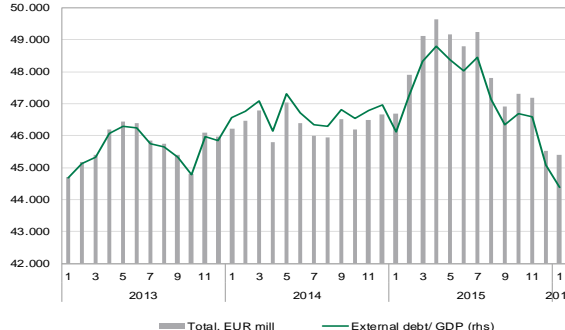
Goods exports and imports (yoy % ch. and mill €)

Source: CBS



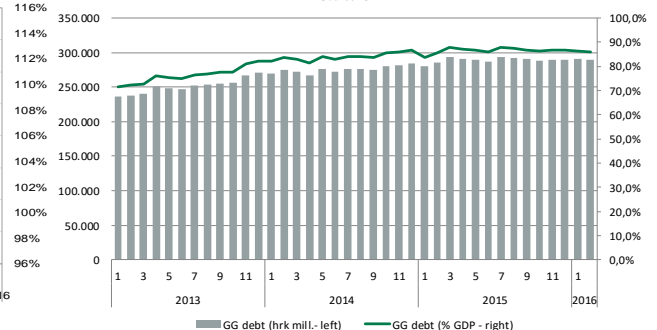
External debt, amount and share to GDP

Sources: CNB, CBS, PBZ



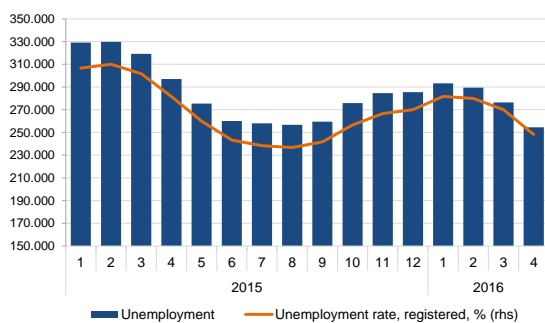
General government debt

Source: CNB



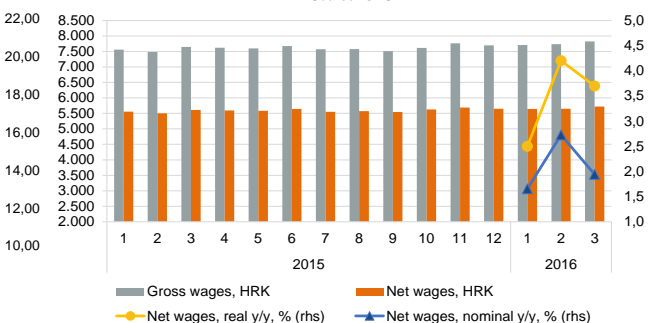
Total unemployment and unemployment rate

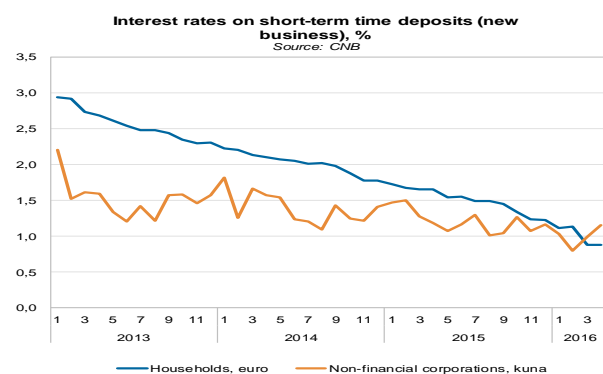
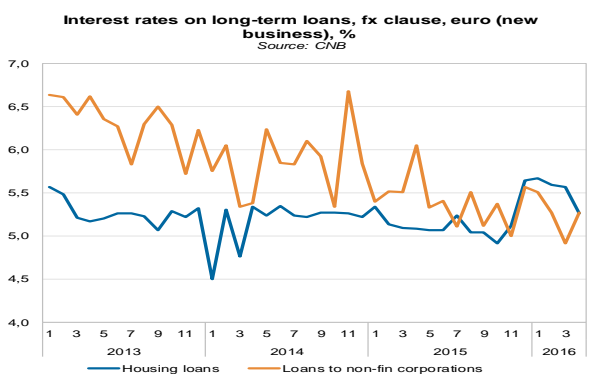
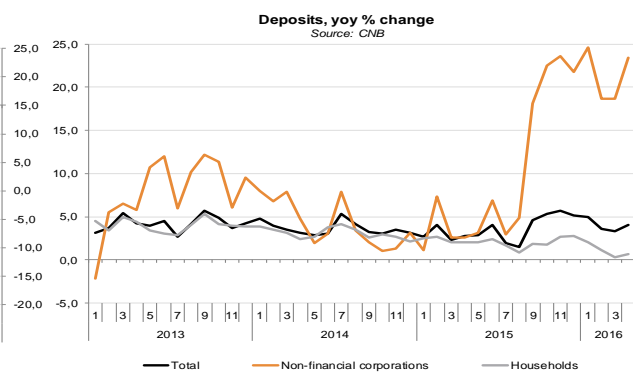
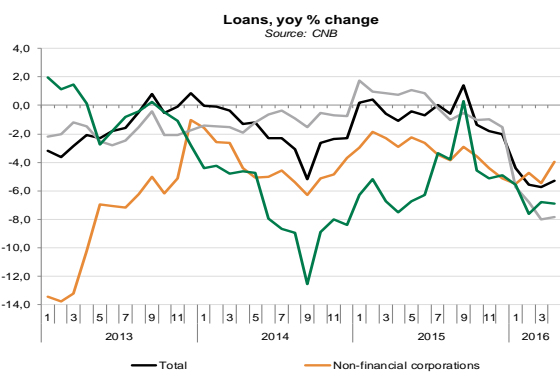
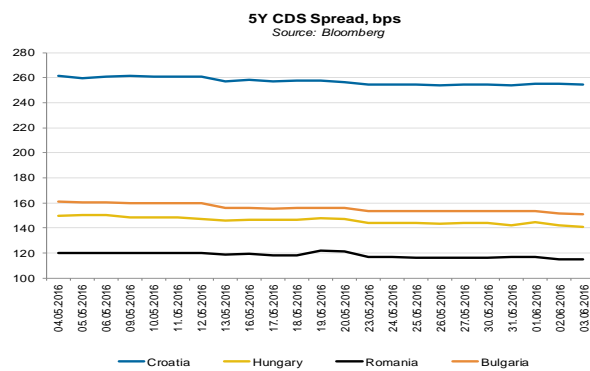
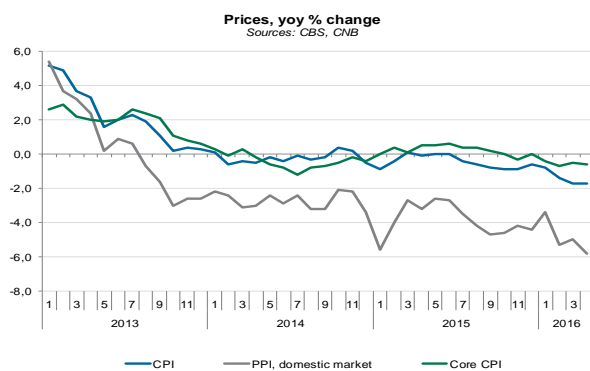
Source: CBS



Wages, monthly average

Source: CBS





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