Information on economic, financial and monetary developments

February 2025

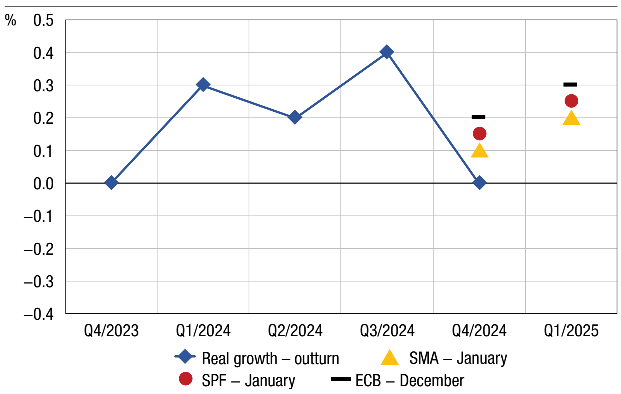
Summary

The euro area economy stagnated in the last quarter of 2024, although it had grown relatively strongly in the previous three months. Economic activity at year-end was weaker than expected, even excluding volatile data for Ireland, which recorded a 1.2% fall. Economic performance was modest across several of the largest euro area economies: Germany's economic activity, for example, contracted by 0.2%, and the French economy recorded an unexpected if slight drop of 0.1%, following strong growth in the summer months, when the Olympics were held. Economic activity in Italy stagnated, but in Spain it continued to grow at a rather strong pace (0.8%) and surprised on the upside in Portugal (1.5%). The adverse developments are in line with monthly confidence indicators, which forecast continued modest growth for the euro area economy, with a pronounced weakness in the manufacturing sector. As regards the first quarter of 2025, most of the available projections point to a gradual recovery (Figure 1). The euro area composite purchasing managers' index (PMI) shifted to the expansion range in January 2025, with the manufacturing indicator showing signs of stabilisation in the contraction range. In contrast, the services sector indicator worsened, but remained in the expansion range.

According to Eurostat's flash estimate, euro area inflation accelerated slightly from 2.4% in December 2024 to 2.5% in January 2025 (Figure 2), which was entirely due to energy inflation increasing from 0.1% in December to 1.8% in January. In contrast, food inflation decelerated from 2.6% in December to 2.3% in January. Core inflation, which excludes energy and food prices, held steady at 2.7% in January, unchanged from the level recorded in the previous four months. Industrial goods inflation held steady at 0.5%, close to the long-term average in the pre-pandemic period. Services inflation slowed down slightly from 4.0% in December to 3.9% in January, but remained relatively high amid the continued strong growth of wages in some service activities. The momentum of overall euro area inflation, an indicator of current inflationary pressures, accelerated to 2.4% in January, mainly due to the strong growth of the momentum of energy inflation, while the core inflation momentum remained at 1.8%.

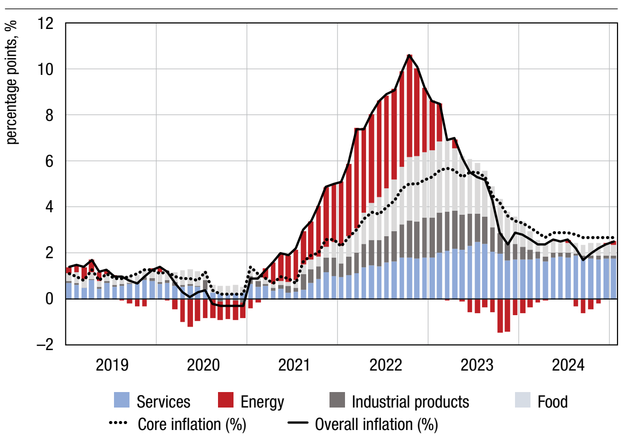
According to monthly data for the fourth quarter of 2024, Croatia's economic activity continued to grow, although somewhat more slowly than in the previous three months. According to the CNB's nowcasting model of economic activity, Croatia's real GDP growth in the fourth quarter could decelerate to 0.6% on a quarterly level, from 0.8% in the third quarter, and to 2.9%, from 3.9% in the third quarter, on an annual level (Figure 3). The continued expansion is primarily driven by an extremely strong growth of domestic demand and favourable developments in trade and construction. The real retail trade turnover rose by 2.1% at the end of the previous year from the quarter before, continuing the growth started at the beginning of 2023. Trade growth was boosted by the strengthening of foreign demand, resulting from the annual growth of tourist arrivals and nights (11% and 10%, respectively) in the fourth quarter, following a weaker performance in the peak tourist season. Construction developments remained favourable, with the sector recording a growth of 3.0% in October and November relative to the third quarter average. The industrial production volume increased at a high monthly rate of 6.3% in December 2024, but

Figure 1 Quarterly growth rates of real GDP in the euro area



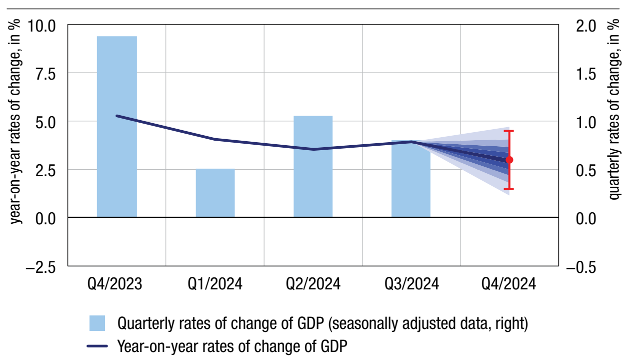
Notes: The abbreviation ECB – December refers to the ECB's December projections of real growth in the euro area. (Broad Macroeconomic Projection Exercise, BMPE). The abbreviations SMA (Survey of Monetary Analysts) and SPF (Survey of Professional Forecasters) refer to the results of the ECB's January 2025 survey of market participants.
Sources: Eurostat and ECB.

Figure 2 Euro area inflation indicators



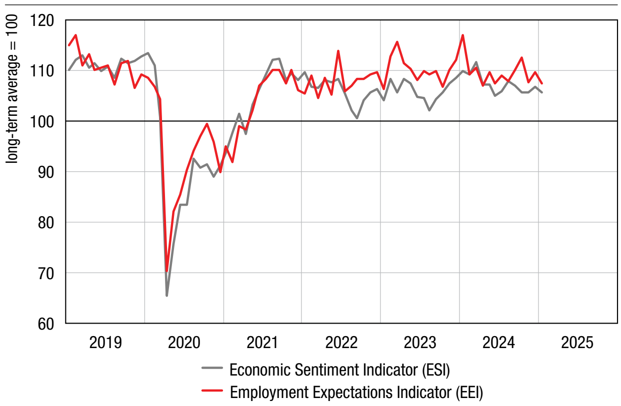
Note: Core inflation is measured by the harmonised index of consumer prices, which excludes energy, food, alcoholic beverages and tobacco prices.
Sources: Eurostat and CNB calculations.

Figure 3 Quarterly gross domestic product



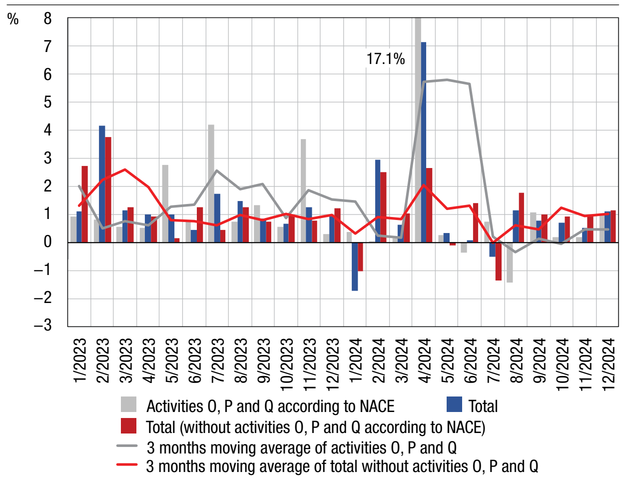
Notes: The estimate for the fourth quarter of 2024 refers to the Monthly indicator of real economic activity of the CNB (for more details on the calculation of the MRGA indicator, see CNB survey Kunovac, D., and B. Špalat: "Nowcasting GDP Using Available Monthly Indicators"). The models are estimated on the basis of data published up to 31 January 2025. The red dot denotes an estimate of the quarterly change in real GDP, with historical errors of estimates within ±1 standard deviation.
Sources: CBS (seasonally adjusted by the CNB) and CNB calculations.

Figure 4 Monthly indicators of economic activity in Croatia



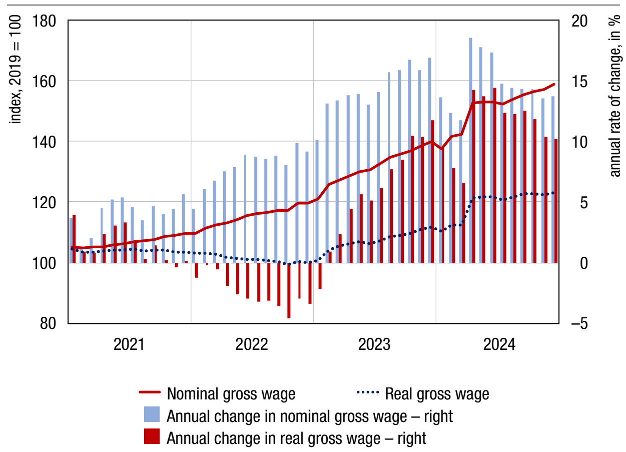
Notes: The economic sentiment index (ESI), and the employment expectation index (EEI) are calculated according to data from business and consumer confidence surveys. For more information, see the methodological guidelines of the European Commission.
Source: EC.

Figure 5 Nominal gross wages
monthly rate of change



Sources: CBS and CNB calculations (seasonally adjusted by the CNB).

Figure 6 Nominal and real gross wages
index, 2019 = 100, annual rate of change



Sources: CBS and CNB calculations (seasonally adjusted by the CNB).

this was not enough to offset the decrease in the previous two months. As a result, industrial production decreased by 0.6% in the fourth quarter of 2024 from the third quarter. The decrease was relatively broadly-based: it was only the production of intermediate goods and energy that grew from the previous quarter's average.

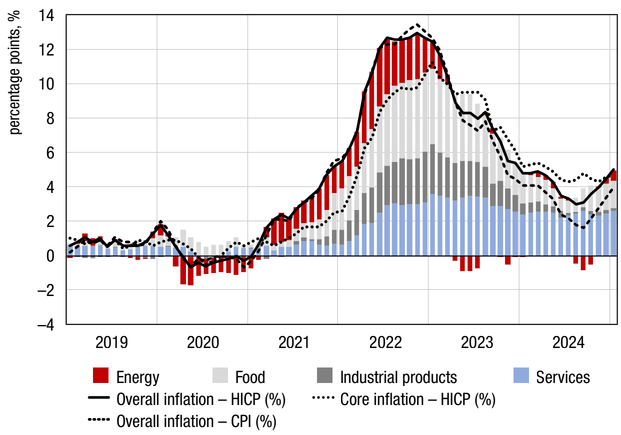
Although most survey indicators of consumer and business optimism in Croatia weakened at the beginning of the first quarter of 2025, they remained relatively high. Trade and service activity indicators weakened the most, but all indicators remained well above their long-term averages. Confidence improved only in industry early in the year, for the second month in a row, exceeding its long-term average. In line with the high levels of business and consumer optimism, the economic sentiment index (ESI) also considerably exceeds its long-term average, and employment is expected to continue growing in most activities (Figure 4).

Employment in the labour market continued to grow at a slower pace in the last quarter of 2024 and the unemployment rate continued to drop, while the nominal wage growth accelerated. The total number of employed persons in Croatia increased by 0.4% in the fourth quarter from 0.9% in the third quarter. Employment in public administration, education, health care and social services (activities O, P and Q) grew by 0.8%, increasing its contribution to total employment growth since April, while employment in the rest of the economy rose by 0.3%. There were slightly over 1.7m employed persons at the end of 2024, 3.6% more than in December 2023. The number of unemployed persons continued to fall in the last quarter of 2024 and was 6.6% lower than in the previous quarter. It dropped to approximately 90 thousand in December 2024, a decrease of 20.4% from the same month in 2023. The registered unemployment rate was below 5% of the labour force in December 2024 (seasonally adjusted data), dropping by 1.3 percentage points from the end of 2023. The average nominal gross wage grew at an accelerated rate of 2.4% in the fourth quarter of 2024 from 0.7% in the third quarter (Figure 5). The growth of wages in activities loosely comprising the public sector (O, P and Q) accelerated to 0.9% and in the rest of the economy to 3.2%. The average nominal gross wage grew at an annual rate of 13.8% in the fourth quarter, compared with 14.5% in the third quarter (Figure 6), up by 20.5% in the public sector and by 11.3% in the rest of the economy. Holding steady in the third quarter, real wages grew by 0.9% in the fourth quarter of 2024 from the average in the preceding three months and by 10.7% from the same period in the previous year.

Inflation in Croatia accelerated in January 2025, largely due to the strengthening of current inflationary pressures in the energy subcomponent, driven by an increase in the administered prices of refined petroleum products and energy, and in the services subcomponent, and to a smaller extent due to adverse base effects. According to Eurostat's flash estimate, inflation in Croatia, as measured by the harmonised index of consumer prices (HICP),[1] picked up to 5.0% in January 2025, from 4.5% in December 2024 (Figure 7). Overall inflation accelerated mainly because of the noticeable acceleration of energy inflation (up to 5.3% from 2.4% in December 2024), primarily arising from the growth of current pressures, while the contribution of adverse base effects was considerably lower. The strong positive current pressures pushed up the annual rate of services inflation

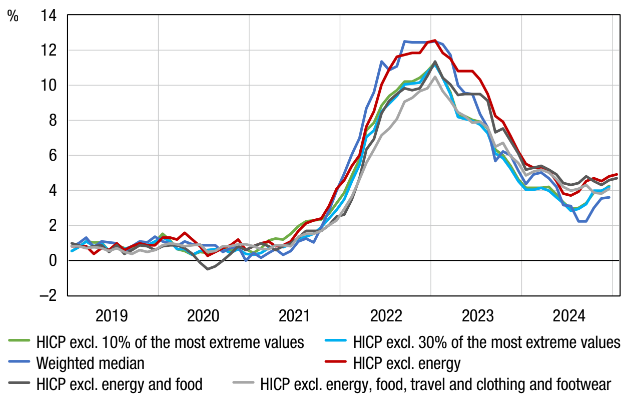
1 Inflation measured by the national consumer price index (CPI), which does not cover the consumption of non-residents and institutional households, picked up from 3.4% in December 2024 to 4.0% in January 2025.

Figure 7 Inflation indicators in Croatia



Note: Core inflation is measured by the harmonised index of consumer prices, which excludes energy, food, alcoholic beverages and tobacco prices.
Sources: Eurostat, CBS and CNB calculations.

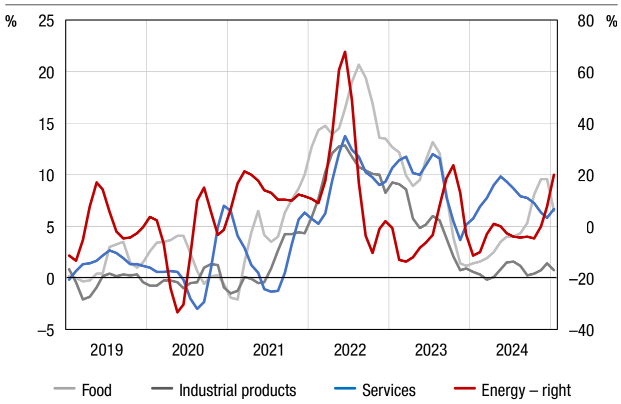
Figure 9 Core inflation indicators



Notes: Trimmed mean eliminates 5% (15%) of components (out of a total of 87 components) with maximum and minimum annual rates of change. The weighted median excludes all values but the weighted median of the distribution of price change.
Sources: Eurostat and CNB calculations.

to 8.2% from 7.7% in December 2024, while food inflation accelerated only slightly, to 5.4% from 5.3% in December, due to unfavourable base effects stemming from a sharp decrease in food prices in January in the previous year. As a result, the momentums[2] of services and energy inflation grew strongly in January, considerably exceeding their usual values (Figure 8). The momentum of food inflation also exceeded its usual values, although it was considerably lower. The momentum of industrial goods inflation also fell in January, standing at low levels, which is an indication of the absence of inflationary pressures in this inflation subcomponent. Core inflation (which excludes energy and food prices) accelerated slightly from 4.6% in December 2024 to 4.7% in January 2025, due to the continued acceleration of services inflation (Figure 9), partly offset by a slowdown in industrial goods inflation (down from 0.8% in December to 0.6% in January). Services thus continue to be a key component of overall inflationary developments in Croatia, contributing 2.6 percentage points to the overall consumer price inflation of 5.0%, while the contribution of food is 1.6 percentage points.

Figure 8 Momentums of the main inflation components



Note: The quarterly rate of change on an annual level has been calculated based on the quarterly moving average of seasonally adjusted harmonised indices of consumer prices.
Sources: Eurostat and CNB calculations.

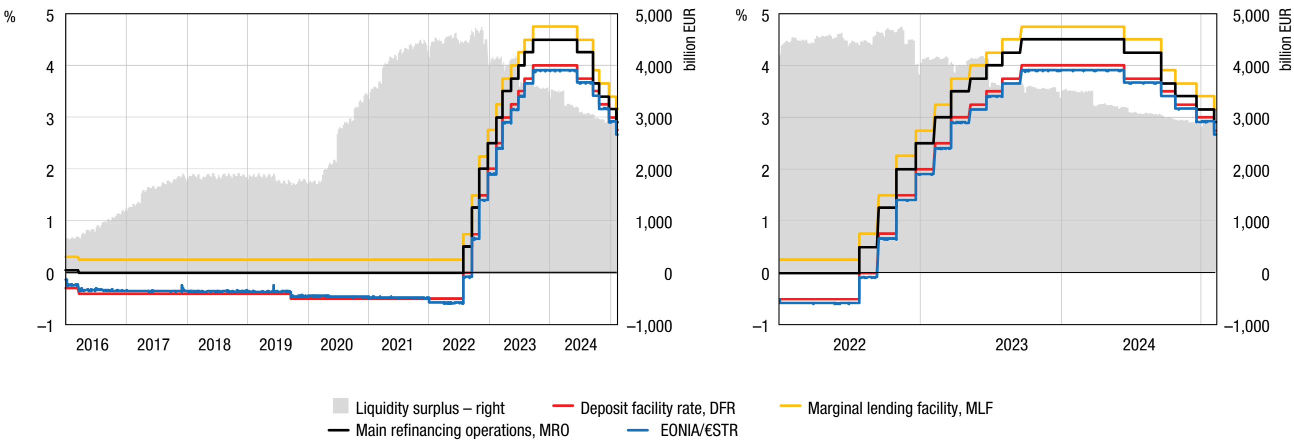
At its meeting on 30 October, the Governing Council of the ECB decided to further gradually moderate the degree of monetary policy restriction (Figure 10). The deposit facility rate, a relevant indicator of the ECB's monetary policy, was set at 2.75% starting from 5 February, a reduction of 25 basis points. The Governing Council noted that the disinflationary process was well on track. However, domestic inflation has remained high, mostly because wages and prices in certain sectors are still adjusting, with a substantial delay, to the past inflation surge. Still, wage growth has decelerated in line with expectations, and corporate profits have offset the impact of the robust growth of labour costs on inflation. The reduction in key interest rates is gradually spilling over to financing conditions, with the result that the borrowing costs of corporations and households are gradually declining. However, with key interest rates still in restrictive territory, new loans largely continue to be granted at higher than existing interest rates, which means that the transmission of the previous tightening of monetary policy to existing loans is still under way. The economy is still affected by headwinds, but the growth of real income and the gradually fading effects of restrictive monetary policy should spur demand over time. The Governing Council is determined to ensure that inflation stabilises sustainably at its 2% medium-term target and it will continue to base its decisions on a data-dependent approach. The Governing Council is not pre-committing to a particular rate path.

The size of the Eurosystem's balance sheet has continued to decrease gradually (Figure 11). On 18 December 2024, banks repaid the remaining amounts borrowed under the targeted longer-term refinancing operations, which concluded this part of the balance sheet normalisation process. The portfolio of securities purchased within the asset purchase programme (APP) and the portfolio of the pandemic emergency purchase programme (PEPP) of the Eurosystem are declining steadily at a measured and predictable pace; the principal payments from maturing securities under the APP have not been reinvested since July 2023 while the reinvestment of the PEPP portfolio was completed at the end of the previous year.

The reduction in key ECB interest rates in January 2025 soon spilled over to interest rates on the money market. In late January, market participants expected key ECB interest rates to continue to be reduced at a lower intensity than in the

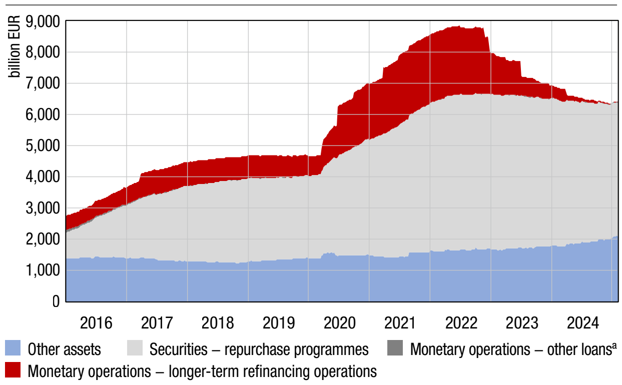
2 Momentum is a short-term inflation indicator, which shows annualised three month-on-three month rates of price change, seasonally adjusted.

Figure 10 Key ECB interest rates



Notes: DFR (deposit facility rate); MLF (marginal lending facility); MRO (main refinancing operations). The EONIA was replaced by €STR in early 2022.
Source: ECB.

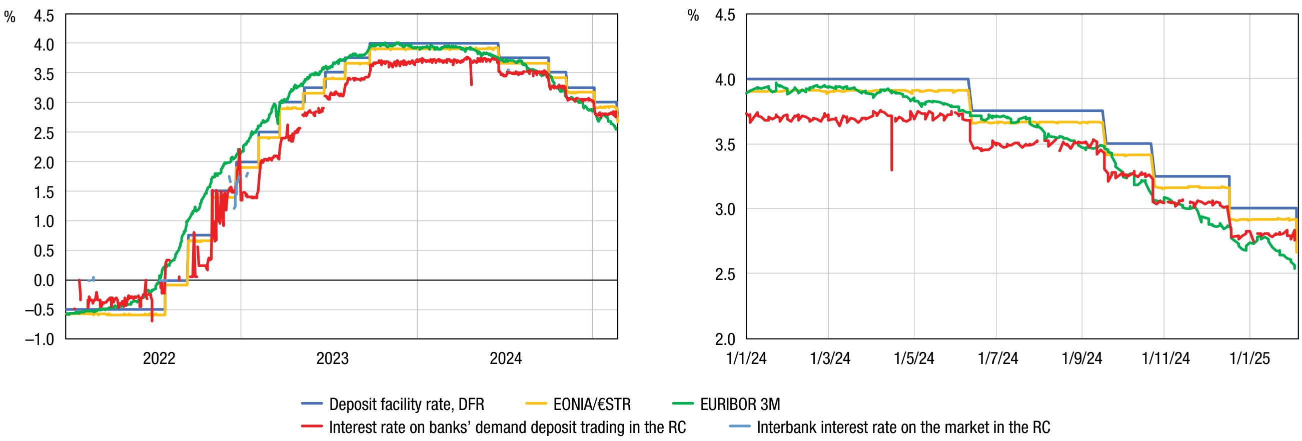
Figure 11 Eurosystem balance sheet



[a] Other loans include main refinancing operations, fine-tuning reverse operations, structural reverse operations, marginal lending facility and credits related to margin calls.
Note: The Eurosystem monetary balance sheet asset items are shown in grey and red and non-monetary in blue.
Source: ECB.

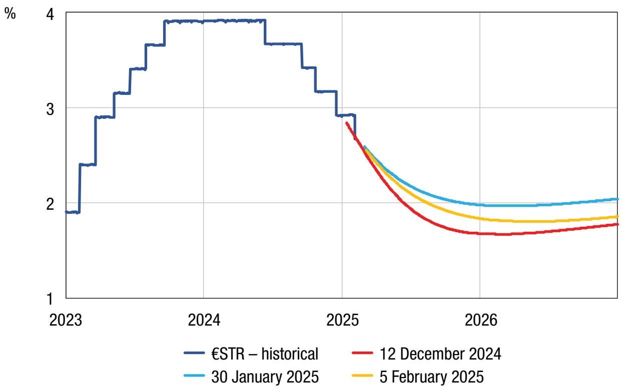
period preceding the December Governing Council meeting, but immediately after the January meeting expectations grew of a sharper interest rate cut. The €STR fell by the amount of reduction in key interest rates (25 basis points) and amounted to 2.7% on 5 February (Figure 12). Similar developments were seen in the Croatian money market, where the overnight interest rate on demand deposit trading fell to 2.5% in early February. As regards market expectations, the €STR forward curve shifted to higher values between the ECB Governing Council meetings in December 2024 and January 2025, dropping to somewhat lower values after the meeting in January (Figure 13). The forward curve shifted to higher values primarily as a result of the transmission of an increase in the US yield curve. This was due to the effect of more favourable data from the US labour market, published on 10 January, and the growth of inflationary expectations, stemming from an increase in crude oil prices and the expected inflationary effects of announced changes in the US trade policy. These factors led to a significant adjustment of market expectations towards slower cuts in the Fed's key interest rates. The change in market expectations towards slower cuts in the ECB's key interest rates also resulted from

Figure 12 Key ECB interest rate and overnight market interest rates in the euro area and Croatia



Notes: DFR (deposit facility rate). The EONIA was replaced by €STR in early 2022. The overnight interest rate on the money market in Croatia in 2022 is based on euro transactions.
Sources: ECB and CNB.

Figure 13 €STR forward curve



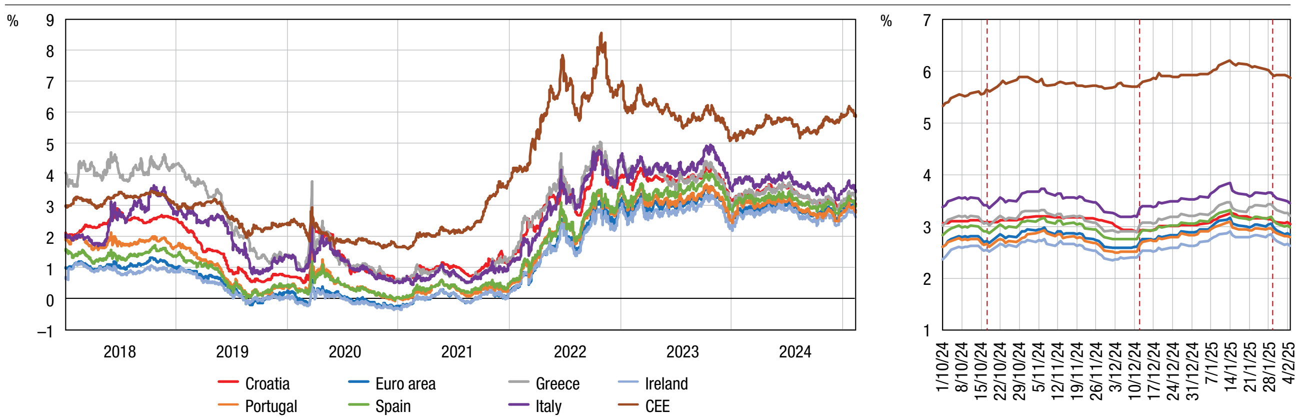
Notes: The forward curve is estimated using the overnight indexed swap rate (OIS). Forward curves show the selected forward curves formed on the day of the ECB Governing Council meeting in December 2024 and January 2025 an on the day of the last available data on 5 February 2025.
Sources: Bloomberg and CNB calculations.

the growth of inflationary expectations for the euro area, influenced to some extent by data on a higher than expected inflation in Spain and Germany, released in late December and early January. However, after the ECB Governing Council meeting in January, market participants started to expect somewhat sharper cuts in the ECB's key interest rates. This could be attributed to weaker-than-forecast data on the economic growth for the euro area, published on 30 January, and growing concerns over potentially negative impacts of the US trade policy, stemming from the announced changes in the US tariff policy towards Canada, Mexico and China and indications that similar measures could soon be applied to the European Union.

Euro area long-term government bond yields rose after the ECB Governing Council meeting in December 2024 and started to decrease gradually in mid-January 2025. Euro area long-term government bond yields grew after the ECB Government Council meeting in December 2024, reaching 3.2% in mid-January 2025 (Figure 14), an increase of 46 basis points, primarily mirroring the growth of yields on long-term US bonds. US long-term government bond yields started to decline in mid-January, followed by euro area long-term government bond yields, which dropped to 2.8% in early February. The decrease in euro area long-term government bond yields in late January and early February was partly due to weak euro area economic indicators released in late January and growing concerns surrounding the impact of the US trade policy on the euro area economy. Croatia's long-term government bond yields closely followed trends in euro area long-term government bond yields, standing at 3.0% at the beginning of February 2025, 13 basis points higher than on the day of the ECB Governing Council meeting in December 2024. In early February 2025, the government issued a EUR 2.0bn eurobond maturing in 2037. The bond bears a yield of 3.3%, with the realised yield slightly lower than that of the last year's ten-year eurobond issue (3.4%).

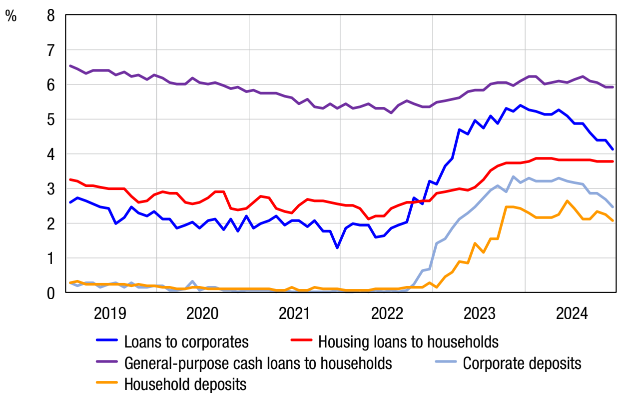
The costs of corporate financing by credit institutions fell to a two-year low in December 2024, while average interest rates on pure new housing loans and general-purpose cash loans to households hovered around the levels from the previous month. The average interest rate on pure new corporate loans stood at 4.14% in December, decreasing by 27 basis points from November (Figure 15), primarily due to a decrease in the average interest rate on working capital loans. In contrast, the cost of household borrowing remained almost unchanged in December from the previous month, amounting to 5.95% for general purpose cash loans and to 3.81% for housing loans. The easing of the restrictive ECB monetary policy continued to be transmitted strongly to corporate financing conditions, with the result that the average interest rate on pure new corporate loans was 129 basis points lower in December 2024 than the highest level recorded during the last monetary policy tightening cycle in December 2023. The interest rate on general-purpose cash loans to households was only 32 basis points lower in December 2024 than at the beginning of the year, while the interest rate on housing loans dropped by 7 basis points from the highest level recorded in April 2024. As regards existing loans, the interest rate on corporate loans decreased by 11 basis points in December, dropping to 4.34%. The interest rate on new corporate loans was thus lower than interest rates on the stock of loans for the third successive month, which opens up the possibility of refinancing existing loans at lower interest rates and stimulates additional decreases in interest rates on existing loans. Interest rates on general-purpose cash loans and housing loans to households held almost steady in December at 6.01% and 3.12%, respectively, reflecting minor changes in interest rates on

Figure 14 Yields on long-term government bonds with the remaining maturity of approximately 10 years



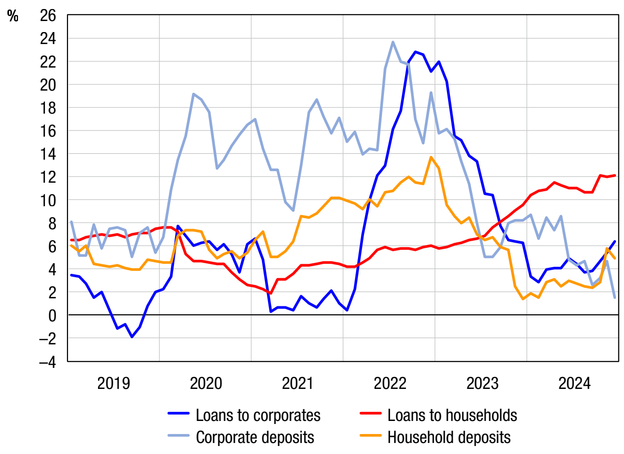
Notes: CEE – countries of Central and Eastern Europe (the Czech Republic, Hungary, Poland and Romania); yields for the euro area and CEE have been weighted by the share of GDP of the countries included. Data from the euro area do not include those from Estonia, Latvia, Luxembourg and Malta. The red dotted lines denote ECB Governing Council meetings in the period of time shown. Last data are for 5 February 2025
Sources: Bloomberg, Eurostat and CNB calculations.

Figure 15 Interest rates on pure new loans and time deposits of corporates and households



Notes: Data up to December 2022 refer to loans and deposits in kuna and currencies indexed to the kuna and in euros, and from January 2023 to loans and deposits in euro. Data refer to pure new loans and deposits. Deposits with a maturity of up to 1 month have been excluded.
Source: CNB.

Figure 16 Corporate and household loans and deposits
year-on-year rates of change, transaction-based



Source: CNB.

existing loans with a fixed interest rate and loans with a variable interest rate indexed to the NRR.

Interest rates on pure new time deposits of corporates and households were lower in December than in the previous month. The average interest rate on pure new corporate deposits decreased by about 20 basis points, dropping to 2.50% (Figure 15) and that on household deposits fell to 2.07%. In December, as in the previous two months, households rescheduled maturing time deposits contracted in late 2023, most of them with one large bank, with maturities between 2 and 3 months and between 6 and 12 months and at interest rates lower than in November, which contributed to a decrease in the average interest rate on pure new household time deposits. Interest rates on existing total corporate and household deposits dropped by 4 basis points (to 0.62%) and by 1 basis point (to 0.48%), respectively. Interest rates on existing time deposits decreased, with slight changes in interest rates on overnight deposits.

Domestic deposits continued to grow in December 2024. Total domestic deposits (excluding the general government) rose by EUR 0.8bn (1.5% transaction-based) in December from November. Overnight deposits increased by EUR 1.0bn, with corporate and household deposits contributing equally to the increase; this rise was offset to a degree by a drop in time deposits (EUR 0.1bn), attributable to corporate deposits (EUR 0.3bn), while household time deposits almost held steady and the deposits of other non-bank financial institutions (mostly investment funds) grew by EUR 0.2bn.[3] The annual growth of total deposits slowed down from 6.5% in November to 4.5% in December 2024 (Figure 16) due to the base effect related to the strong growth of all domestic sectors' deposits in December 2023, which significantly exceeded their growth in December last year. Household overnight and time deposits increased the most, while the stock of overnight corporate deposits decreased at the end of 2024 from the end of 2023 and corporate time deposits grew at a decelerated rate. After corporate and household time deposits peaked in May and June 2024, respectively, the share of corporate deposits in total deposits gradually fell to 25.6% in December and the share of household deposits went down to 27.4% in the same month.

Corporate loans continued to grow in December 2024 and so did household loans, led by housing loans, while general-purpose cash loans increased less than in the previous months of 2024. Loans to domestic sectors (excluding the general government) rose by EUR 0.3bn (0.8%, transaction-based), reflecting the continued growth of corporate lending (EUR 0.2bn). Household loans also continued to grow, rising by EUR 0.1bn, but their growth was slightly weaker than in the previous months, due primarily to a slowdown in general-purpose cash loans. Corporate loans grew at an accelerated annual rate from 5.5% in November to 6.4% in December (Figure 16). Excluding the effect of the repayment of one large company's syndicated loan from January 2024, the annual growth rate of corporate loans in 2024 was 8.2%. Household lending increased at an only slightly accelerated annual rate, up from 12.0% in November to 12.1% in December (transaction-based), with housing and general-purpose cash loans growing at the same rate as in November (9.1% and 15.9%, respectively). However, excluding the impact of a large bank acquiring credit card issue in October, the annual growth rate of household loans accelerated from 11.0% in November to 11.1% in December. The momentum[4] of loans strengthened additionally in December. The momentum of housing loans also accelerated (to 10.3%), exceeding the annual growth rate, whereas the momentum of general-purpose cash loans fell below the annual growth rate to 12.5%.

3 In December, citizens invested EUR 546m in the eighth issue of government securities maturing in 3 months, with an option to reinvest almost EUR 400m from matured treasury bills purchased in September. The stock of these securities increased by EUR 150m in December, reaching EUR 4.2bn, the highest level national securities have reached since the government launched the issue.

4 Momentum is a short-term indicator of lending activity which shows annualised three months-on-three months rates of change in loans.