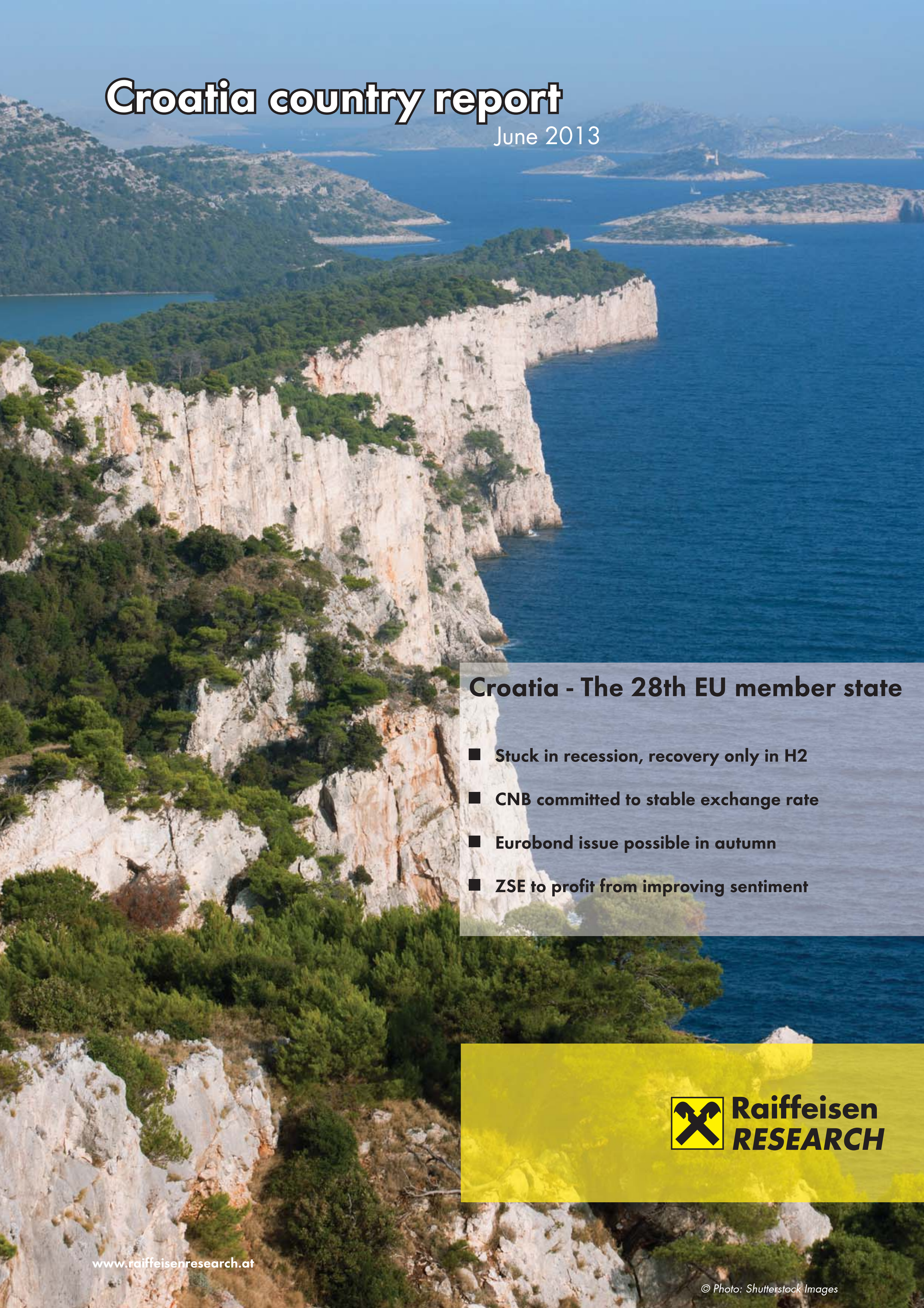


Croatia country report

June 2013

Croatia - The 28th EU member state

- Stuck in recession, recovery only in H2
- CNB committed to stable exchange rate
- Eurobond issue possible in autumn
- ZSE to profit from improving sentiment

Raiffeisen RESEARCH

www.raiffeisenresearch.at

Content

Explanation:
e ... estimate
f ... forecast
p ... preliminary figures

Abbreviations

Currencies and Countries

ALL	Albanian lek
BAM	Bosnian marka
BGN	Bulgarian lev
BYR	Belarusian roubel
CZK	Czech koruna
EKK	Estonian kroon
HUF	Hungarian forint
HRK	Croatian kuna
LTL	Lithuanian litas
LVL	Latvian lats
PLN	Polish zloty
RON	Romanian leu
RSD	Serbian dinar
RUB	Russian rouble
SIT	Slovenian tolar
SKK	Slovak koruna
TRY	Turkish lira
UAH	Ukrainian hryvnia

Economic abbreviations

%-chg	Percentage change (not in percentage points)
avg	average
bp	basis points
C/A	Current Account
CPI	Consumer Price Index
FDI	Foreign Direct Investments
FX	Foreign Exchange
FY	Full year
GDP	Gross Domestic Product
LCY	Local Currency
mmav	month moving average
mom	month on month
pp	percentage points
PPI	Producer Price Index
qoq	quarter on quarter
T/B	Trade Balance
ULC	Unit Labour Costs
yoy	year on year
ytd	year-to-date

Stock Exchange Indices

BELEX15	Serbian stock index
BET	Romanian stock index
BUX	Hungarian stock index
CROBEX10	Croatian stock index
PX	Czech stock index
MICEX	Russian stock index
SASX-10	Bosnian stock index
WIG 20	Polish stock index

Equity related

DY	Dividend yield
EG	Earnings growth
LTG	Long term (earnings) growth
P/E	Price earnings ratio
RS	Recommendation suspended
UR	Under Revision
Eurozone	*Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, Netherlands, Portugal, Slovenia, Slovakia, Spain*
CE	*Central European countries - Poland, Hungary, Czech Republic, Slovakia, Slovenia*
SEE	*South East European countries - Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Kosovo, Romania, Serbia*
CIS	*European CIS (Commonwealth of Independent States) countries - Russia, Ukraine, Belarus*
CEE	*Central and Eastern Europe (CE + SEE + CIS)*

Highlights

Croatia, the 28th EU member country, applied for EU membership in 2003 and conducted negotiations from 2005 until 2011, when the accession treaty was signed. In the long, exhausting negotiation process, Croatia adopted the acquis communautaire. Hence, non-residents face no obstacles to investing in Croatia since all capital restrictions have been removed. However, global uncertainty and local obstacles are preventing stronger inflows of foreign capital. In order to attract foreign investments administrative hurdles must be removed, the competitiveness of Croatian economy must be improved and fiscal sustainability and credibility need to be assured. In the pre-crisis years, foreign capital was mostly directed to non-tradable sectors, which had a negative effect on industrial production and created an illusion of prosperity that was supported by increased consumption.
Fiscal policy credibility remains one of the major obstacles. The public sector accounts for about half of GDP, but it is mostly inefficient. In the past few years, the government has mostly failed to restructure the public sector, which led to accelerating public debt growth amidst economic decline. Currently, there are numerous initiatives in the EU aimed at strengthening fiscal and economic balance and revealing potential macroeconomic imbalances. They emphasise harmonisation of fiscal and structural policies, stronger budgetary control of national budgets by the European Commission, early warning systems as regards macroeconomic imbalances and ex-ante and ex-post sanctions.
As budget revenue collection is not proceeding as the government had hoped, financing needs are high. With the new recovery plan for the general and district hospitals due to their inability to service their liabilities, the government will need roughly an extra HRK 5 bn, which also supports our expectations of two more bond issues this year (besides the local one in summer, we expect a placement on the international market in autumn). The risk premium is currently rather low for a country with a sub-investment credit rating, amidst strong liquidity on the global markets. With negative real returns on the core markets, Croatian Eurobonds offer a solid yield without threat of default.
The state-owned bank (Hrvatska Postanska Banka) and insurance company (Croatia Osiguranje) are in the process of privatisation and the government has announced the sale of their share in hotels, as well as real estate in their ownership. There have been rumours that Croatia Airlines is seeking for a strategic partner. Furthermore, the government is seeking advisors to propose the best model for granting concessions for publicly owned motorways, to help reduce public debt and repay the loans taken out for highway construction.

Key economic figures: Croatia

	2008	2009	2010	2011	2012	2013e	2014f
Nominal GDP (EUR bn)	47.5	44.8	44.4	44.4	43.9	45.5	47.0
Real GDP (% yoy)	2.1	-6.9	-2.3	0.0	-2.0	-0.5	1.0
Industrial output (% yoy)	1.2	-9.2	-1.4	-1.2	-5.5	-1.5	2.0
Producer prices (avg, % yoy)	8.3	-0.4	4.3	6.4	7.0	3.0	3.5
Consumer prices (avg, % yoy)	6.1	2.4	1.1	2.3	3.4	3.2	3.0
Avg gross industrial wages (LCY, % yoy)	7.0	0.8	0.0	1.3	1.9	-1.0	0.0
Unemployment rate (avg, %)	13.2	14.9	17.4	18.0	19.1	19.8	19.5
General budget balance (% of GDP)	-1.4	-4.1	-4.9	-5.0	-4.1	-4.2	-3.8
Public debt (% of GDP)	29.3	35.8	42.2	46.7	53.7	59.5	62.1
Current account balance (% of GDP)	-9.0	-5.1	-1.1	-0.9	0.1	-0.3	-0.5
Official FX reserves (EUR bn)	9.1	10.4	10.7	11.2	11.2	11.3	11.5
Gross foreign debt (% of GDP)	85.4	101.0	104.6	103.0	102.3	100.0	98.9
EUR/HRK (avg)	7.22	7.34	7.29	7.43	7.52	7.55	7.50
USD/HRK (avg)	4.91	5.26	5.49	5.34	5.85	5.68	5.64

Source: Thomson Reuters, CNB, CBS, Raiffeisen RESEARCH

Recommendations
(Horizon: March 2014)

Bond markets
Buy
HRK 2y T-bonds
HRK 3y T-bonds
EUR-linked T-bond (2014)

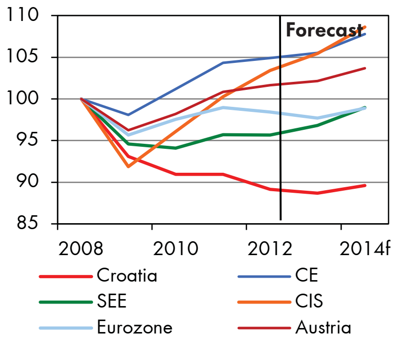
HRELEC 2017 USD
(spread trade to CROATI 2017 USD: enter above 80bp, exit at 50bp)

Equity market

Buy
SETX index certificate
(AT0000A00BF2)

Hold
Podravka

Real GDP Index (2008=100)



Source: Eurostat, Thomson Reuters, Raiffeisen RESEARCH

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EU accession – opportunity for enervated economy

- **EU membership as a great opportunity and challenge**
- **High political stability, despite half decade of recession**
- **No need for IMF and European assistance**

Politics

A year and a half has passed since the last parliamentary elections. Despite the leading position of the Socialist Democratic Party (SDP) on the scale of preferred political parties, the continued loss of support for the governing coalition is undeniable, largely driven by the prolonged crisis and the resulting high unemployment, especially among the young. There has been a mild rise in the popularity of the Croatian Democratic Union (HDZ), which is still burdened by court proceedings from the previous mandate. The political stability of the country remains high and is likely to be maintained until the next parliamentary elections at the end of 2015 or at the beginning of 2016. On the other hand, it is evident that during this term of government Croatia will not see a more significant economic recovery since the period of the crisis has not been used to implement structural changes as preconditions for sustainable growth and development, especially now as new EU member. With the prolonged recession and continued economic decline, the crisis cannot be addressed by fiscal stimulus, maintaining the status quo, a lack of reforms and large public infrastructural projects. Firstly, this is because the crisis in Croatia is of a structural nature and secondly because the unsustainable dynamics, now paired with the high level of public debt, limits the operation of fiscal policy. Finally, despite the downgrade of its rating to below investment grade, it is evident that Croatia will not seek IMF and European assistance. Croatia has no problems with liquidity so the role of these institutions would be a good excuse to implement reforms amidst quite strong resistance from the unions of public servants and various social and interest groups.

EU integration

Almost 12 years after its road to the EU started, Croatia's EU membership as the 28th member of the EU has been fixed (1 July 2013). In the long, exhausting negotiation process, Croatia adopted the acquis communautaire, meaning that it fulfilled all of the requirements needed for harmonisation with the EU. With the long negotiations and the fact that the entry date has been known for many months, we do not expect any major changes from one day to the next. There are numerous initiatives in the EU aimed at strengthening Croatia's fiscal and economic balance and revealing potential macroeconomic imbalances. They emphasise harmonisation of fiscal and structural policies, stronger budgetary control of national budgets by the European Commission, early warning systems for macroeconomic imbalances and ex-ante and ex-post sanctions. EU funds represent an opportunity for stronger economic growth. Sectors that should be strongly in focus include: renewable energy, irrigation projects, waste management, WWTP (waste water treatment plants), water supply, sewerage and infrastructure projects in the transport sector (reconstruction of railway lines, international corridors and border crossings). There is also potential in tourism and agriculture (food production), especially in combining those two sectors. However, the main instruments for a better future can be found only within Croatia, as higher and more sustainable growth depends on reforms and the creation of a more competitive economy.

Political parties in Parliament

Ruling coalition	Party leader
Socialdemocratic Party (SDP) - 59	Zoran Milanović
Croatian Citizens's Party (HNS) - 14	Vesna Pusić
Istrian Democratic Party (IDS) - 2	Ivan Jakovčić
Croatian Pensioners Party (HSU) - 4	Silvano Hrelja
Opposition parties	
Croatian Democratic Union (HDZ) - 42	Tomislav Karamarko
Croatian Peasant Party (HSS) - 1	Branko Hrg
Independent Democratic Serb Party (SDSS) - 3	Vojislav Stanimirović
Bosnian Democratic Party of Croatia (BDSH) - 1	Nedžad Hodžić
Croatian Democratic Alliance of Slavonia and Baranja (HDSSB) - 7	Vladimir Šišljagić
Croatian Labourists - Labour Party - 6	Dragutin Lesar
Croatian Civic Party (HGS) - 2	Željko Kerum
Croatian Party of Rights dr. Ante Starčević - 1	Ruža Tomašić

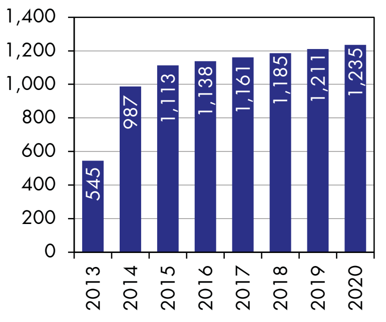
Source: Political parties

Position in public office

Function	Name	Party affiliation
President of the Republic	Ivo Josipovic	
Prime Minister	Zoran Milanovic	SDP
President of the Parliament	Josip Leko	SDP

Source: Government, Parliament, Office of the President

Structural and cohesion funds*



** planned allocation for Croatia, in EUR mn*
Source: European Commission, Croatian Chamber of Commerce

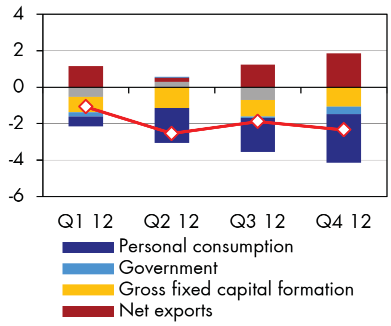
Still waiting for recovery

- **Half of a decade of negative economic performance**
- **Structural problems remain**
- **Lower external vulnerability**

The fourth successive year of economic decline is behind us. The year ahead will mark a half of a decade of the downward trend in Croatia's economy. As compared to 2008, GDP is cumulatively lower by some 11%, with personal consumption and investments accounting for the largest negative contribution. Considering the structural weaknesses of Croatia's economy and lack of strong reforms, paired with the very fragile, insecure external environment, we think the government's projected growth of 0.7% has again been set too high, as it is based on investments (predominantly public) which are directed to non-tradable sectors. Our expectations, as well as first quarter indicators, reflect further economic decline, with more prominent negative developments in the first half of the year, while in the second half we are expecting to see a mild recovery thanks to a good tourist season, stabilisation in the European market and realisation of some of the long-announced public investments.
In order to attract private investments it is necessary to create a stimulating investment climate by removing a series of administrative hurdles, alleviating the tax burden, making the labour market more flexible and reforming public services, which is needed to achieve greater efficiency and make them work for the market.

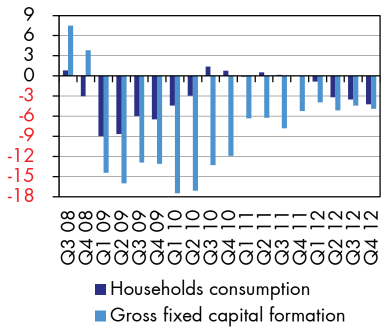
At the annual level, personal consumption will continue to fall, burdened by high pessimism and continued deleveraging. Household income has been diminished by the increase in the tax on consumption and administratively managed prices of services rendered by the public sector, as well as by declining employment. The activity rate decreased to 59.7% at the end of 2012 and has been accompanied by speedy growth in the number of unemployed. The spike in the number of the unemployed according to the ILO methodology indicates a reduction in the gray (informal) economy, as a consequence of the substantial progress in the collection of tax and other government revenues. The reduction in the degree of tax evasion and gray economy increases fairness in government financing paired with a one-off increase in the budget revenues. However, without the concurrent reduction in tax rates it has resulted in an increase in the overall tax burden for the economy, deepening the recession. In the medium term, personal consumption (as the largest GDP component) will not be the driving force behind economic growth, but a mere follower. This reduces the need for the imports of goods and hence external vulnerability measured by the current account balance will be reduced to a minimum. This opens up the possibility of strengthening the competitiveness of the export sector, which only manages to soften the negative trends in the domestic market, due to the narrow and unfavourable basis. Therefore, in addition to restoring the credibility of fiscal policy, one of the priorities for economic policy-makers is to create the preconditions for the development of a competitive industry (with high value added), which would replace a share of imports but also be competitive in the EU markets and the markets of third countries. This could have a positive influence on GDP and improve the share of goods exports in GDP, which has been on a long trend of stagnation for many years.

Contributions to GDP growth



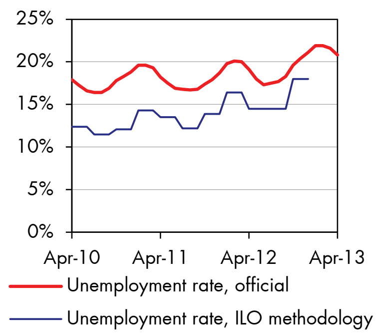
Source: CBS, Raiffeisen RESEARCH

Investments & household consumption



Real growth rates (% yoy)
Source: CBS

Unemployment

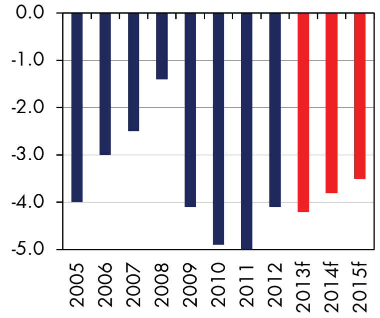


Source: CBS, CES

Risks of even higher deficit

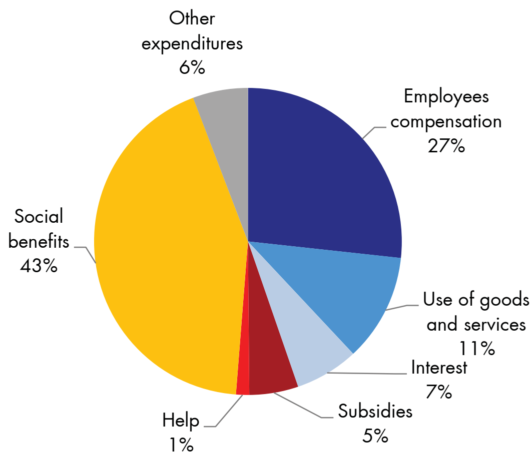
- **Narrow tax base and weak recovery imply lower budget revenues**
- **No changes in the structure of expenditures**
- **Unsustainable dynamics of public debt growth**

General budget balance (% of GDP)



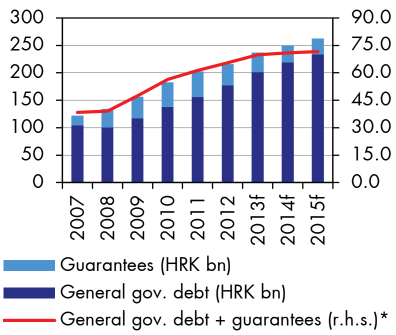
** ESA 95*
Source: MoF, Raiffeisen RESEARCH

Structure of government expenditures



Data for year 2012
Source: MoF

General government debt



** in % of GDP*
Source: MoF, Raiffeisen RESEARCH

Although the general government deficit in 2012 dropped significantly (by almost 1 pp, from 4.5 to 3.6% of GDP, GFS 2001), due to better revenue collection the expenditure side of the budget maintained the unpopular status quo. 2013 featured an unpleasant surprise and divergence from the proclaimed goal and the economic and fiscal policy guidelines adopted several months earlier, in the summer of 2012. As a consequence, credit rating agencies (S&P, Moody's) downgraded Croatia's credit rating to non-investment grade, citing divergence from fiscal consolidation, the lack of reforms, weak competitiveness and poor chances of recovery as the reasons. Negative consequences from the rating downgrade may be felt over the medium term (3-5 years) in the form of a higher debt repayment burden and lower potential economic growth rate.

Budget revenues fell in the first quarter due to the decline in business activity and consumption, which reduced the tax base despite an improvement in revenue collection. The decline in budget revenues resulted in a budget revision in April already. The desired consolidation on the expenditure side of the budget and specific structural measures to achieve long-term sustainability were not seen. Moreover, there are no significant savings as regards the expenses of the central government and the greatest changes have to do with the so-called other items. The expenditure reduction at the level of the consolidated general government and the consequential deficit decline from HRK 13.2 bn to HRK 11.5 bn was almost entirely achieved through smaller capital investments of extra-budgetary agencies (Croatian Waters, Croatian Roads) in the overall amount of HRK 1 bn. On the other hand, revenues are based on the expected GDP growth of 0.7%, which we think is overly optimistic, so there is a real danger of revenues falling short. According to our expectations, the consolidated general government deficit will be higher than the official projections by roughly 0.5 p.p. of GDP, due to several reasons. We expect GDP to fall, in real terms, by at least 0.5%, implying an even larger shortfall in income (by some HRK 1 bn). Expenditure realisation is uncertain, especially as regards expenditures for employees and social contributions, and thus we expect higher expenditures than envisaged in the budget revision. As a result, if the dynamics of government spending do not change the annual deficit might go up by some HRK 1.6 bn.

General government debt at the end of 2012 totalled HRK 177 bn, equivalent to almost 54% of GDP. Including guarantees, i.e. potential public debt, which will most likely become part of the debt of the central government, this share climbs to 70.4%. Although public debt growth dynamics will weaken in 2013, the growth rate will remain high (exceeding 10%) and consequently Croatia's public debt is expected to reach 60% of GDP. This is the level set by the Maastricht criteria and

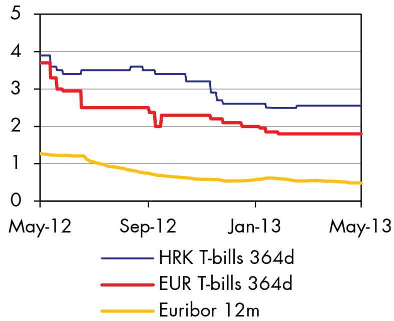
Period of high liquidity and easing pressures

- **High liquidity and minimal interest rates**
- **Easing inflationary pressures at the beginning of the year**
- **Adjustment to EU prices at a high level**

High liquidity and interest rates at minimum levels were maintained in the first part of 2013. In addition to the average daily kuna liquidity of HRK 5.5 bn, overnight deposits held at the rate of 0.25% by commercial banks at the central bank steadily rose. As a direct consequence of this growth, the central bank decided to reduce the remuneration rate calculated on overnight deposits of commercial banks to 0.0%. The Croatian National Bank continued to pursue a monetary policy aimed at preserving price stability by maintaining a stable exchange rate of the kuna against the euro. The central bank is ready to use foreign exchange interventions and other administrative measures to defend the EUR/HRK exchange rate, even at the expense of lower liquidity, i.e. rising interest rates. The reasons for such a policy can primarily be sought in the high euroisation and import dependence of the domestic economy. As long as the EUR/HRK exchange rate remains stable, the monetary authority will adhere to its policy of high primary liquidity enabling interest rates to remain minimal, along with yields on MoF T-bills. Following Croatia's EU accession the central bank will be faced with certain institutional adjustments as well as financial commitments that need to be met. The Croatian National Bank will become a full participant in the Eurosystem's core activities, giving up monetary sovereignty, but participating in the decision-making process and all tasks related to monetary policy at the Eurosystem level. We do not expect Croatia to join the monetary union until 2018 (after accession Croatia needs to spend at least two years in ERM II).

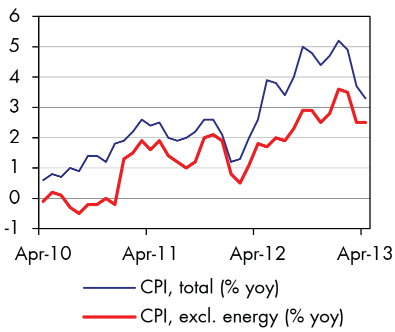
Despite weak domestic demand and relatively stable crude oil prices, inflation in 2012 was strongest in the last four years, as a consequence of the increase in the VAT rate (in March), the spike in regulated prices (gas and electricity, in May) and food products, resulting from the unfavourable weather. Inflationary pressures continued at the beginning of this year, but with less intensity. By the end of the year, when the basis effect is eliminated, the inflationary pressures will subside. Pressures on the demand side are lacking, as seen in the development of producer's prices at the beginning of the year. Inflationary pressures in the Eurozone are also mild, and crude oil prices are stable and thus import prices are not contributing to growth in domestic prices. Due to Croatia's high dependence on imported energy, however, the risk of prices changing due to possible geopolitical turmoil is always present. A possible increase in food prices is also a source of risk, which depends on the weather. Croatia's EU accession is not expected to be followed by sudden inflationary shocks, especially taking into consideration the high level of adjustment of consumer prices in Croatia to those in the EU, which is currently at around 80%. The necessary adjustments, i.e. convergence of individual prices, will be carried out gradually in the medium term, probably accompanied only by partial spikes in the prices of certain product groups and/or services. An assessment of future movements in prices of basic product groups shows that Croatia should not expect any sizeable growth in the prices of consumer goods, non-alcoholic beverages, clothes and shoes because they already are at levels similar to those in the EU. Inflationary pressures will primarily be felt in services (education, recreation, culture) and housing, and to a lesser degree energy.

Interest rates (%)



Source:Thomson Reuters, CNB, MoF

Consumer prices (% yoy)



Source: CBS, Raiffeisen RESEARCH

Money market outlook

	curr*	Sep-13	Dec-13	Mar-14
ZIBOR 3m (eop)	1.29	1.6	1.5	1.9
ZIBOR 12m (eop)	2.63	3.2	3.1	3.2

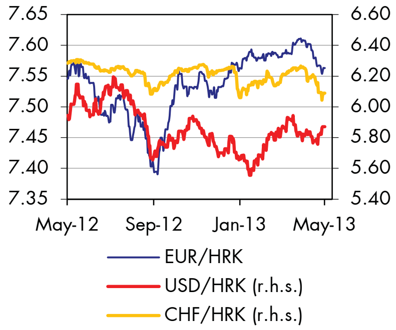
	2011	2012	2013e	2014f
ZIBOR 3m (avg)	3.2	3.4	1.4	2.5
ZIBOR 12m (avg)	4.4	4.6	3.0	3.4

** 27 May 2013, 5:00 p.m. CET*
Source: Thomson Reuters, Raiffeisen RESEARCH

Slow EUR/HRK growth with external imbalances reducing

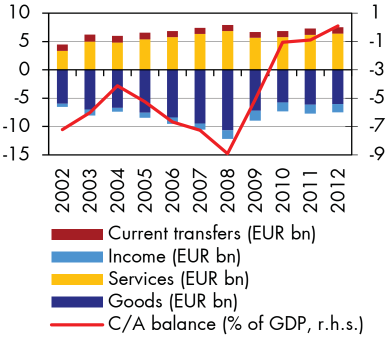
- **No fundamentals for kuna appreciation in 2013**
- **Stable exchange rate is the CNB's priority**
- **Private sector deleveraging and weak domestic demand limit external debt growth**

Exchange rate development



Source: CNB

Current account balance



Source: CNB, Raiffeisen RESEARCH

Exchange rate outlook

	current[1]	Sep-13	Dec-13	Mar-14
EUR/HRK[2]	7.56	7.55	7.60	7.57
USD/HRK[2]	5.85	5.68	5.63	5.61
EUR/USD[2]	1.29	1.33	1.35	1.35
	2011	2012	2013e	2014f
EUR/HRK[3]	7.43	7.52	7.55	7.50
USD/HRK[3]	5.34	5.85	5.68	5.64
EUR/USD[3]	1.39	1.29	1.33	1.33

1) 27 May 2013, 5:00 p.m. (CET)
2) eop
3) average
Source: CNB, Raiffeisen RESEARCH

Due to deleveraging by the domestic private sector vis-ŕ-vis foreign creditors and weak inflows of foreign capital, the average EUR/HRK exchange rate in 2012 was only 1.1% higher than in 2011 and volatility measured by standard deviation was the lowest since 2007. Domestic sector demand for foreign currency and the increase in bank reserves for NPLs will exert upward pressure on the EUR/HRK in 2013. The CNB's anticipated tightening of regulations relating to bank reserves support expectations that the usual seasonal strengthening of the kuna during the tourist season will be softened. Nevertheless, as always, market players' awareness that the CNB is committed to its stable exchange rate policy will prevent a more prominent rise in EUR/HRK and dampen uncertainty and volatility in the FX market. The CNB has sufficient funds for FX interventions since the foreign borrowings of the government increase its FX reserves. In addition to inflows from tourism and the CNB's commitment to preserve exchange rate stability, the borrowing of (public) enterprises and possible inflows of foreign capital due to the spurring of investments might temporarily cause HRK to strengthen against EUR and lead to a departure from the usual seasonal developments.

The higher exchange rate contributed to the competitiveness of Croatian products abroad, thus favourably influencing the current account (C/A) in the balance of payments. Following the relatively high C/A deficit in the pre-crisis years, which resulted from strong imports of durable consumer goods, the deficit narrowed in the past four years as a result of slack domestic demand. Imports of goods remain substantially lower than in the pre-crisis years, while exports recovered, after having fallen in 2010. The narrowing of the deficit on the goods account paired with the growth in revenues from tourism in 2012 led to the first C/A surplus on an annual level since data collection started in 1999. Mostly due to the lack of recovery in domestic demand for imported products, we expect that this year will again be relatively favourable for developments in the C/A in the sense of maintaining the deficit in the goods account at below pre-crisis levels and increasing the surplus in the services account. However, developments in the trade of goods might be slightly more unfavourable than last year (due to the temporary loss of preferred treatment in CEFTA members) so the C/A might reflect a mild deficit in 2013.

Domestic private sector deleveraging has impacted external debt, the nominal amount of which declined last year. However, its share in GDP mildly increased (to 102.3%). The crisis thus contributed to halting the strong growth in external debt which financed spending in the pre-crisis period, due to the lack of domestic capital. In addition to improving the C/A position, this reduced the economy's external imbalance. The only sector with a considerable contribution to the growth of external debt is the government sector. Private sector deleveraging might continue but at a slower pace than in the previous year, considering that bank deleveraging is expected to slow down. The strongest pressures on external debt growth are again expected to come from the government. International reserves should continue their mild upward trend, positively affecting the coverage of short-term debt maturity by international reserves. Said indicator improved from 73% at the end of 2011 to 89% at the end of 2012, and the positive trend is expected to continue throughout this year.

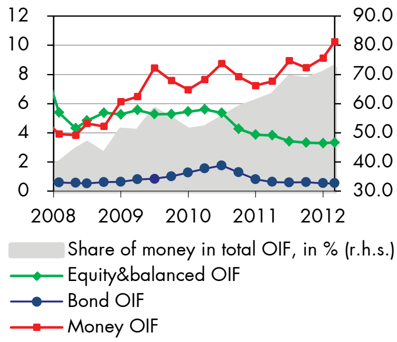
Bank profitability declines

- **Growth in bad loans to enterprises accelerates**
- **Accelerated deleveraging of bank groups connected by ownership**
- **Banking sector – profit falls but capital adequacy increases**

The last year's operating results of the financial sector were marred by the unfavourable developments in the domestic economy and changed financing conditions on foreign capital markets. The fund industry is dominated by mandatory pension funds, which managed some 73% of total fund assets as at the end of last year. Domestic government bonds make up some two thirds of mandatory fund assets. The increase in bond prices as a result of reducing risk aversion on foreign financial markets enabled pension funds and thus the fund industry to boast two-digit annual yields. Operating results in the banking sector suffered from the rise in risk provisions. The deepening recession in the economy increased the share of problem loans to total loans to 24.7%. Negative developments in the corporate segment picked up pace in October when regulations on financial operation came into force. In addition to regulating deadlines for payments among corporate and between the corporate and the government sector, they also laid down conditions for mandatory initiation of pre-bankruptcy settlement among debtors and creditors, i.e. initiation of bankruptcy proceedings if they fail to reach a settlement. The domestic market is burdened by recession and numerous corporate cannot adjust their operations to the shorter deadlines for payment. Their inability to comply with regulatory requirements results in mandatory initiation of pre-bankruptcy settlement and impaired value of creditor receivables. For credit institutions, this leads to the need for additional reserves due to asset impairment, with a negative effect on the operating results in the current period. As a result of increased risk provisions, the return on invested bank capital fell, and thus the 2012 average return of the banking sector was 4.8%. The unpredictable effect of pre-bankruptcy settlements on their operations reduced the credit demand of solvent enterprises. However, last year marked a turning point. Bank corporate loans went down by 12.8% due to the transfer of loans to recovered shipyards to the government sector and borrowing of a share of large enterprises directly abroad, as well as repayment of loans to domestic banks. Faced with client deleveraging, banks reduced their sources of financing. The funds obtained from owners remained at the same level and consequently the decline in risky assets pushed up the capital adequacy coefficient to 20.6%. At the same time, funds stemming from debt went down. Since Croatian banks have predominantly borrowed from financial groups to which they are linked by ownership, the reduction in the sources of funds was mainly reflected in their debt to their owners. Over the last year it went down by 22.1%.

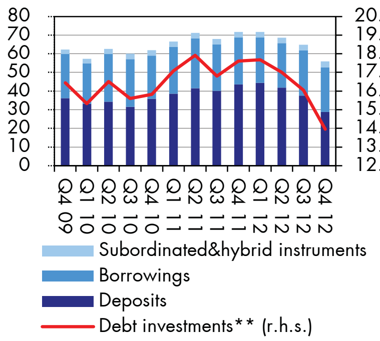
This year we do not expect any major changes in demand for loans and financial services. An increase in borrowing might occur only from the government sector, if it fails to realise its plan of borrowing in the foreign markets. As a result, the level of financial sector assets is expected to stagnate and bank deleveraging with foreign owners is expected to lose some momentum compared with the previous year.

Open-end investment funds*



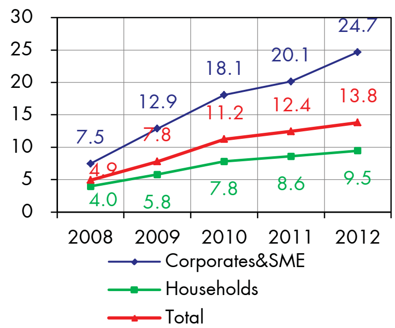
** net assets, HRK bn*
Source: CFSSA

Debt investments (HRK bn)*



** from foreign parent banks to Croatian banks*
*** as % of total assets*
Source: CNB, Raiffeisen RESEARCH

Non-performing loans (eop, %)

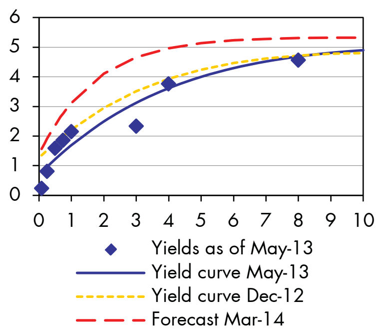


Source: CNB

Investment rating lost, declining yields spurred by ample liquidity

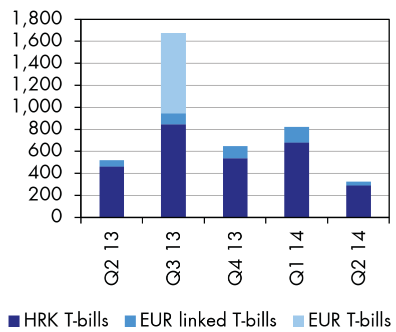
- **High refinancing needs imply new borrowings**
- **Yield declines due to high liquidity, not improved fundamentals**
- **Need for higher fiscal transparency**

HRK yield curve (%)



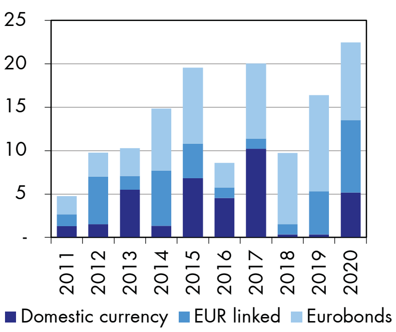
Source: Bloomberg, Raiffeisen RESEARCH

Treasury bills maturities (EUR mn)*



* *as of 7- May*
Sources: MoF, Raiffeisen RESEARCH

Outstanding bonds (HRK mn)



Sources: MoF, Raiffeisen RESEARCH

The announced and then postponed international bond issue denominated in USD in the US market was finally realised late in March. The issue was worth 1.5 bn, had a coupon of 5.5% and average yield at issue of 5.625%. The demand for the Croatian issue exceeded supply by five times, which is not surprising considering the ample liquidity in the international capital markets and low returns offered by safe havens such as American and the German debt securities. In addition, the activity of CEE countries in the Eurobond market decreased substantially relative to 2012, when placements of regional bonds exceeded EUR 20 bn in Q1, which was twice the amount seen in Q1 2013. On the other hand, the market was dominated by relatively unfavourable conditions due to the elevated insecurity in Europe's periphery, e.g. Italy's inability to form a government after the parliamentary election and the crisis in Cyprus. Together with ample liquidity and clear message from the main central banks that they will strive to support recovering markets and economies by pursuing low interest rate policies, the second quarter was marked by Croatian yields dropping to historic lows and the CDS returning to below 300bp. However, the narrowing of spreads should be attributed entirely to market conditions and not to any improving fundamentals in the Croatian economy.

The review of the yield changes and risk premiums indicates Croatia's increased vulnerability to global developments relative to other countries in the region, especially compared to Central European countries (apart from Slovenia and Hungary). This should largely be attributed to the below investment rating and very poor fundamentals, i.e. poor chances of an economic recovery and the significantly undermined credibility of fiscal policy. In the coming quarters, Croatian Eurobonds will follow regional developments which, on the one hand, might come under pressure from poor chances of economic growth, insecurity about the outcome of the debt crisis in Europe's periphery and, on the other hand, renewed risks of rating downgrades of some countries (Slovenia and Hungary). If there are no major tensions in the market and global sentiment gradually stabilises and then even improves in the second half of the year, the longest Croatian ten-year issues might remain at around 300bp.

As expected, in Q1 the domestic market was marked by modest turnovers with more activity at the currency clause curve. Pure kuna issues found themselves in the focus of investors after the CNB additionally contributed to the increase in kuna liquidity, by lowering the overnight interest rate on deposits with the central bank. Due to continued inflows of capital into the portfolios of certain institutional investors (pension funds) and regulatory requirements compelling them to invest at least 50% of their assets in government bonds, the shallow local market is unable to satisfy demand which works in favour of government issues.

One of the key problems of the debt market in Croatia (both short and long term) continues to be the lack of a calendar of issues in the primary markets. This also creates problems for the secondary market, limiting investors in the pursuit of their investment strategies, and consequently suffocating the secondary market.

In general, bond issues are large and scarce, creating one-off bouts of ample supply, which overwhelm investors at one moment only to create a lack of government papers for investors to invest in the subsequent period. The share of non-residents in the local market is still very small. However, due to the attractive returns in comparison to yields in the region and in the context of Croatia's pending accession to the EU, their share might increase slightly.

Developments in yields on domestic issues will depend on the evolution of the Eurobond curve. The maturing kuna issue worth HRK 4 bn in July paired with weak inflows to the state budget and generally high refinancing needs (maturing syndicated loans of commercial banks totalling some EUR 900 mn) imply the possibility of another summer issue in the domestic market. Demand will, no doubt, be good. We also expect two more bond issues, one denominated in euro and one in kuna, in a total value of EUR 1.5 bn, with 5- to 10-year maturity. In addition, we believe it is possible that Croatia may once again turn to international capital markets in the autumn. Finally, as the MoF announced that the shortfall in budget will be closed with a planned local issuance of HRK 5 bn in the last quarter 2013.

Next year will be slightly more demanding as regards bond repayment and accompanying coupons since the maturity of the Eurobond in April of 2014 (EUR 500 mn) is closely followed by the local euro issue, worth EUR 650 mn, in June. In the context of high refinancing needs and lack of transparency as regards government borrowing, we expect the government to remain active in 2014, both in the domestic and the foreign market, while the existing loans to the government with commercial banks and short-term debt resulting from issued T-bills will probably be renewed through the same instruments.

The long-standing ample kuna liquidity in the money market continues, enabling the government to continue with its practice of issuing short-term securities, T-bills, under very favourable conditions. T-bill interest rates hit minimum levels in December and have not increased since then. It is worthy of note that short-term debt arising from the issued T-bills indexed to the euro has been shifting more towards pure kuna securities. Short-term debt arising from issued T-bills totalled HRK 29 mn at the end of May, i.e. 8.5% of estimated GDP, which was up some 2.2 bn compared to the situation at the end of December last year.

It is realistic to expect such market developments to continue in the months ahead. Moreover, although the main aim of the lowering of the interest rate on overnight deposits with the central bank was said to be the redirection of released assets to the placements to the private sector, we do not expect credit activity to pick up substantially. The market has been dominated by ample liquidity over the last three years but weak demand, the fragile economy and high risk aversion prevented more active lending by commercial banks. This measure will, however, have a favourable influence on fiscal policy, i.e. on T-bills, whose yields might stay at their historic lows in these conditions.

As long as the EUR/HRK exchange rate remains stable, the monetary authorities will continue to conduct the policy of high primary liquidity, enabling minimum interest rates but also yields on the MoF T-bills. The relatively cheap borrowing of the central government is supported by the demand of domestic market participants which found themselves lacking more attractive investments. The maturing euro T-bill in mid-August, worth EUR 730 mn, will most likely be settled as part of the possible issue of bonds in the domestic capital market.

HRK yields outlook (%, ask)

	current[1]	Sep-13	Dec-13	Mar-14
1 year T-bill yield[2]	2.60	2.70	2.80	3.00
3 year T-bond yield[2]	3.61	3.90	4.10	4.20
5 year T-bond yield[2]	4.06	4.10	4.40	4.50
10 year T-bond yield[2]	4.55	5.30	5.40	5.50
	2011	**2012**	**2013e**	**2014f**
1 year T-bill yield[3]	4.02	4.07	2.80	3.50
3 year T-bond yield[3]	6.75	4.88	3.86	4.20
5 year T-bond yield[3]	6.46	5.51	4.10	4.40
10 year T-bond yield[3]	6.64	5.78	5.35	5.55

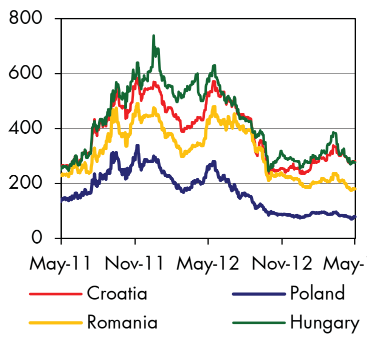
1) 27 May 2013, 05:00 p.m. (CET); 2) % eop; 3) % avg
Source: Thomson Reuters, Raiffeisen RESEARCH

Rating comparison*

	S&P	Moody`s	Fitch
Poland	A-	A2	A-
Hungary	BB	Ba1	BB+
Czech Rep.	AA-	A1	A+
Slovakia	A	A2	A+
Slovenia	A-	Ba1	BBB+
Romania	BB+	Baa3	BBB-
Bulgaria	BBB	Baa2	BBB-
Croatia	**BB+**	**Ba1**	**BBB-**

** long-term, FCY, on 27 May*
Source: rating agencies, Raiffeisen RESEARCH

CDS spread (USD, bp)

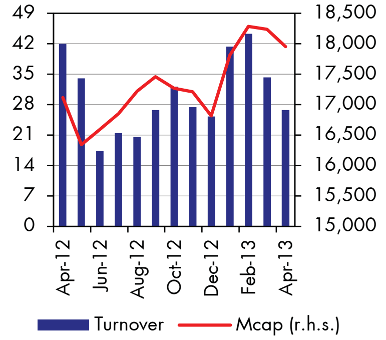


Source: Bloomberg

EU accession cushions weak macroeconomic outlook

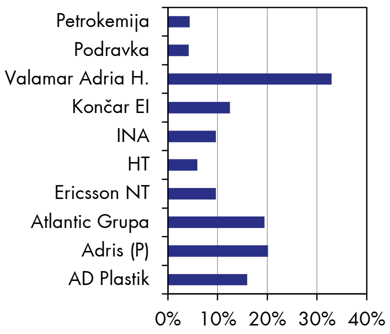
- We expect positive sentiment on regional equity markets to last until end-2013
- CROBEX10 is relatively attractively valued, with a 2013e P/E ratio of 9.1x
- EU accession should decrease the market's risk perception and hence some stronger capital inflows are expected

Turnover and Mcap of ZSE (EUR mn)



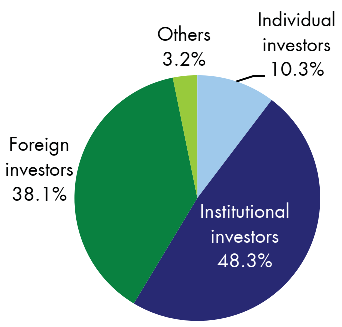
Source: ZSE

Ytd perf. of CROBEX10 members



Source: ZSE

Investors' structure on ZSE



Source: CDA

Structure of the Croatian equity market

Croatian equity market is one of the smallest and least liquid markets in CEE terms. There are 181 companies listed on Zagreb Stock Exchange, all of which are local companies. When it comes to investor structure, foreign investors account for 38.1%, whereas 48.3% are domestic institutional investors (as of April 30, 2013, CDA). The CROBEX10 index covers 10 blue-chip stocks. The main heavyweights are the oil company Ina (index weighting: 20.42%), followed by Hrvatski Telekom (19.87%), preferred shares in Adris Grupa (15.76%) and Končar Elektroindustrija (10.51%). These four shares have an index weighting of 66.5%. The broader CROBEX consists of the 25 most liquid stocks.

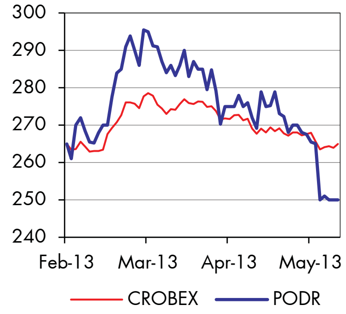
Current situation and market outlook

We expect the positive sentiment on regional equity markets to last until the end of 2013, supported by recovery in the US and Eurozone economies as well as in the CEE region in H2 2013. Moreover, risk aversion is weakening globally and therefore we expect local factors to gain importance again. Overall, we favour cyclical stocks. Within the CEE region the strongest performance is expected for the Turkish ISN National 100 index, which should profit from the expected Turkish credit rating upgrade by Moody's in H2 2013. The Croatian equity market started the year quite well, as the CROBEX10 index recorded the strongest surge in the CEE region in Q1 2013, with a gain of 14.7%. As the macro situation was not very supportive, we ascribe investors' optimism to the nearing EU accession and the high liquidity in the system. Total regular equities turnover amounted to HRK 1.1 bn in the first four months of the year, down 17.9% yoy. Total market capitalisation on the ZSE was HRK 136.5 bn at end-April 2013. The CROBEX10 is relatively attractively valued with an estimated P/E ratio of 9.1x for 2013, despite the strong advance in Q1 2013. In our view, the rationales for low valuation are the weak economic situation and very slow reforms. Still, although the Croatian economic outlook is not very promising, EU accession in July should decrease the market's risk perception and hence some stronger capital inflows are expected. For the remainder of the year, we expect further positive performance by the CROBEX10, but the growth rates seen in Q1 2013 are not likely to be repeated, as they are not fundamentally justified in our opinion. One of the key drawbacks of Croatian market is the still very low liquidity.

Podravka (Hold, TP HRK299)

Podravka is the largest branded food producer in CEE. Podravka has associated companies and subsidiaries in 18 countries and food and pharmaceuticals production facilities located in Croatia, Poland, Czech Republic and B&H. The management board adopted a new strategic plan in December 2012, according to which the management plans to put their efforts into gross margin enhancement through product mix improvement. Recently, in an AGM notice the company proposed a simplified reduction of the share capital, which would be performed by a decrease in the nominal value of the share. The reason is the coverage of the previous years' losses. The shareholders will also decide on the amendments of the company's statutes, which would enable the management and supervisory board to independently decide on capital increases. Furthermore, the state would lose the right to independently appoint two supervisory board members. If the amendments are accepted, it could mean the entrance of new investors if the state does not take part in the potential capital increase. In the future, Podravka plans to grow through organic growth, acquisitions and strategic partnerships with other food companies in the region.

Podravka

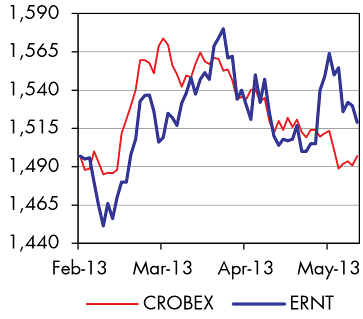


Source: ZSE, Raiffeisen RESEARCH

Ericsson NT (Reduce, TP HRK 1,368)

Ericsson Nikola Tesla is an integral part of the Ericsson group and within the corporate organisation is part of the Region Western & Central Europe. The company operates primarily in Croatia, neighbouring countries and the CIS region. Ericsson NT is the leading regional ICT solution provider. The company's activities include marketing and sales, R&D, design of the total communications solutions, services in the multi-service and mobile networks area and complex system integration. Posted figures for Q1 2013 outperformed our estimates at all levels. The management mentions intensive sales activities related to the modernisation of mobile networks with customers in CIS region, and hence we might see some more positive surprises in coming period. The key advantage is the excellent liquidity situation and strong cash flows, which have enabled company to regularly pay quite high dividends (HRK 170 for 2012). However, in line with decreasing profitability due to rising competition, we do not reckon with such hefty dividends as were paid in the past for more than a few years.

Ericsson Nikola Tesla

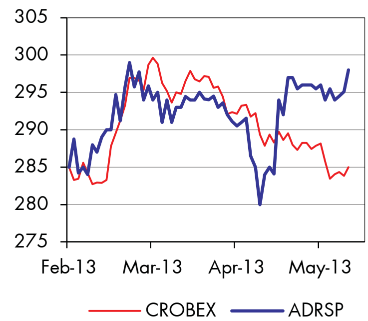


Source: ZSE, Raiffeisen RESEARCH

Adris (U.R. (Hold), TP U.R. (HRK 263)

Adris Group mainly operates in three segments: tobacco, tourism and retail. TDR holds a market share near 70% of the Croatian cigarette market and is an important player in the region. Croatian iNovine and Opresa (B&H) kiosk chains make up a retail unit. iNovine manages around 400 sales outlets across the country, and Opresa has 260 outlets in B&H. The tourism segment is organised in Adria Resorts which holds Maistra. The accommodation portfolio consists of 9 hotels (1,783 rooms), 8 tourist settlements (2,062 rooms) and 7 camps (7,606 sites). These units are located in Istria and around 60% of the capacities are categorised as 4* and 5*. The stock's main advantage is its extremely attractive valuation of 3 EV/EBITDA and the hefty cash position. Tourism business results improved significantly in 2012 and Q1 2013, but on the other hand the tobacco segment exhibits continuously negative trends. The Croatian Ministry of Finance proposed a new system of excise taxes on cigarettes and tobacco. The new tax regime will have an adverse impact on the tobacco unit's performance, especially as the highest price increase refers to the cheapest brands, which brings them closer to the price of competitors' products. Further growth in excise taxes is expected in 2014 to 2018, related to Croatia's EU accession.

Adris Grupa (P)



Source: ZSE, Raiffeisen RESEARCH

Real GDP (% yoy)

Countries	2011	2012	2013e	*Consensus*	2014f	*Consensus*
Poland	**4.3**	**1.9**	**1.2**	*1.4*	**2.5**	*2.8*
Hungary	**1.6**	**-1.7**	**0.0**	*-0.1*	**1.5**	*1.3*
Czech Rep.	**1.7**	**-1.2**	**-0.2**	*-0.1*	**1.8**	*1.7*
Slovakia	**3.2**	**2.0**	**0.9**	*1.0*	**2.5**	*2.4*
Slovenia	**0.6**	**-2.3**	**-1.0**	*-1.3*	**1.0**	*0.5*
CE	**3.1**	**0.5**	**0.6**	*0.7*	**2.1**	*2.2*
Croatia	**0.0**	**-2.0**	**-0.5**	*-0.4*	**1.0**	*1.4*
Bulgaria	**1.8**	**0.8**	**0.5**	*1.2*	**2.5**	*2.2*
Romania	**2.2**	**0.7**	**2.0**	*1.7*	**2.5**	*2.6*
Serbia	**1.6**	**-1.7**	**1.0**	*1.4*	**2.0**	*3.0*
Bosnia a. H.	**1.0**	**-1.3**	**0.5**	*0.8*	**2.0**	*2.5*
Albania	**3.1**	**1.6**	**2.0**	*2.1*	**3.5**	*3.3*
SEE	**1.7**	**0.0**	**1.2**	*1.2*	**2.2**	*2.4*
Russia	**4.3**	**3.4**	**2.0**	*3.2*	**3.0**	*3.8*
Ukraine	**5.2**	**0.2**	**1.0**	*0.9*	**3.0**	*3.5*
Belarus	**5.3**	**1.5**	**3.0**	*2.8*	**4.0**	*3.5*
CIS	**4.4**	**3.1**	**2.0**	*3.0*	**3.0**	*3.8*
CEE	**3.7**	**2.0**	**1.5**	*2.2*	**2.7**	*3.2*
Turkey	**8.5**	**2.2**	**4.0**	*3.9*	**4.5**	*4.8*
Austria	**2.7**	**0.8**	**0.5**	*0.6*	**1.5**	*1.5*
Germany	**3.1**	**0.9**	**0.5**	0.7	**1.8**	1.7
Eurozone	**1.5**	**-0.5**	**-0.7**	*-0.4*	**1.2**	*0.9*
USA	**1.8**	**2.2**	**1.5**	*2.1*	**2.5**	*2.7*

Source: wiiw, Raiffeisen RESEARCH

Consumer prices (avg, % yoy)

Countries	2011	2012	2013e	2014f
Poland	4.3	3.7	1.2	2.2
Hungary	3.9	5.7	2.3	2.8
Czech Rep.	1.9	3.3	1.9	2.0
Slovakia	3.9	3.6	2.2	2.5
Slovenia	1.8	2.6	2.5	2.3
CE	**3.6**	**3.8**	**1.7**	**2.3**
Croatia	2.3	3.4	3.2	3.0
Bulgaria	4.2	3.0	3.1	3.4
Romania	5.8	3.3	4.6	3.3
Serbia	11.3	7.8	10.0	9.0
Bosnia a. H.	3.7	2.1	2.0	2.1
Albania	3.5	2.0	2.5	3.0
SEE	**5.5**	**3.7**	**4.5**	**3.8**
Russia	8.5	5.1	6.2	5.8
Ukraine	8.0	0.6	1.8	7.5
Belarus	53.2	59.2	20.0	17.5
CIS	**9.7**	**6.3**	**6.3**	**6.3**
CEE	**7.5**	**5.3**	**4.7**	**4.8**
Turkey	6.5	9.0	6.0	6.0
Austria	**3.6**	**2.6**	**1.9**	**2.0**
Germany	2.5	2.1	1.5	1.5
Eurozone	**2.7**	**2.5**	**1.5**	**1.6**
USA	3.2	2.1	1.5	2.0

Source: Thomson Reuters, Raiffeisen RESEARCH

Current account balance (% of GDP)

Countries	2011	2012	2013e	2014f
Poland	-4.9	-3.5	-3.0	-3.9
Hungary	0.8	1.6	1.6	2.1
Czech Rep.	-2.8	-2.4	-2.1	-2.0
Slovakia	-2.0	2.2	2.9	2.9
Slovenia	0.0	2.4	2.7	1.3
CE	**-3.1**	**-1.8**	**-1.4**	**-1.9**
Croatia	-0.9	0.1	-0.3	-0.5
Bulgaria	0.3	-0.7	-1.6	-2.3
Romania	-4.5	-3.8	-3.0	-3.0
Serbia	-9.3	-10.7	-9.6	-9.6
Bosnia a. H.	-9.5	-9.7	-9.8	-9.9
Albania	-11.3	-8.8	-9.1	-9.2
SEE	**-4.4**	**-4.2**	**-4.0**	**-4.1**
Russia	5.1	3.7	2.7	1.9
Ukraine	-6.3	-8.5	-6.5	-5.7
Belarus	-8.6	-2.9	-5.6	-7.3
CIS	**3.9**	**2.6**	**1.8**	**1.0**
CEE	**0.9**	**0.8**	**0.4**	**-0.2**
Turkey	-10.0	-6.1	-6.7	-6.3
Austria	**1.4**	**1.8**	**1.0**	**0.9**
Germany	5.7	5.8	5.5	5.5
Eurozone	**0.1**	**1.2**	**1.4**	**1.4**
USA	-3.1	-3.0	-2.8	-2.5

Source: Thomson Reuters, Raiffeisen RESEARCH

General budget balance (% of GDP)

Countries	2011	2012	2013e	2014f
Poland	-5.0	-3.9	-4.1	-3.8
Hungary	4.3	-1.9	-2.9	-2.9
Czech Rep.	-3.1	-4.9	-3.0	-2.6
Slovakia	-4.9	-4.3	-2.9	-2.4
Slovenia	-6.4	-4.0	-3.5	-3.2
CE	**-3.4**	**-3.9**	**-3.6**	**-3.3**
Croatia	-5.0	-4.1	-4.2	-3.8
Bulgaria	-2.1	-0.5	-2.1	-1.7
Romania	-5.6	-2.9	-2.8	-2.5
Serbia	-4.5	-5.7	-4.5	-4.0
Bosnia a. H.	-1.3	-2.0	-1.5	-1.0
Albania	-3.5	-3.0	-3.0	-3.0
SEE	**-4.5**	**-3.0**	**-3.1**	**-2.7**
Russia	1.6	0.4	0.4	-1.0
Ukraine	-4.3	-5.5	-4.0	-3.0
Belarus	2.4	0.5	-1.0	0.0
CIS	**1.2**	**0.0**	**0.0**	**-1.1**
CEE	**-0.8**	**-1.5**	**-1.4**	**-1.9**
Turkey	-1.4	-2.4	-2.2	-2.5
Austria	**-2.5**	**-2.5**	**-2.6**	**-1.8**
Germany	-0.8	0.1	-0.5	0.0
Eurozone	**-4.2**	**-3.7**	**-2.9**	**-2.8**
USA	-8.7	-7.0	-5.3	-3.7

Source: Thomson Reuters, Raiffeisen RESEARCH

Public debt (% of GDP)

Countries	2011	2012	2013e	2014f
Poland	56.4	56.1	56.1	53.8
Hungary	80.6	79.2	78.9	78.0
Czech Rep.	40.8	45.8	47.9	48.9
Slovakia	43.3	52.1	54.9	55.8
Slovenia	46.9	54.0	65.0	67.0
CE	**54.7**	**56.6**	**57.8**	**56.9**
Croatia	46.7	53.7	59.5	62.1
Bulgaria	16.3	18.3	17.8	19.4
Romania	34.7	37.8	38.4	38.7
Serbia	45.8	59.7	61.2	59.9
Bosnia a. H.	39.2	42.0	42.1	39.6
Albania	59.4	61.5	62.6	62.0
SEE	**36.1**	**40.9**	**42.3**	**42.8**
Russia	9.8	10.5	11.0	11.5
Ukraine	36.0	36.8	38.0	38.5
Belarus	48.5	31.5	31.0	30.3
CIS	**12.9**	**13.1**	**13.6**	**14.1**
CEE	**27.5**	**28.7**	**29.5**	**29.6**
Turkey	39.1	36.8	35.0	33.0
Austria	**72.5**	**73.4**	**75.6**	**75.2**
Germany	80.5	81.7	81.0	78.7
Eurozone	**87.3**	**90.6**	**95.5**	**96.0**
USA	98.7	103.1	106.3	107.3

Source: Thomson Reuters, Raiffeisen RESEARCH

Gross foreign debt (% of GDP)

Countries	2011	2012	2013e	2014f
Poland	67.2	71.3	70.9	69.6
Hungary	132.5	126.8	119.1	106.3
Czech Rep.	48.8	49.6	50.2	49.9
Slovakia	76.3	71.2	69.9	74.7
Slovenia	111.0	111.3	111.1	110.5
CE	**75.3**	**76.0**	**74.8**	**72.7**
Croatia	103.0	102.3	100.0	98.9
Bulgaria	93.1	96.4	93.3	92.9
Romania	75.2	75.2	69.8	67.6
Serbia	77.6	86.9	84.3	80.9
Bosnia a. H.	67.1	63.1	62.2	61.0
Albania	23.6	24.7	24.5	26.6
SEE	**79.3**	**80.5**	**76.6**	**74.8**
Russia	30.4	30.7	31.0	32.0
Ukraine	77.4	76.3	76.6	71.7
Belarus	61.1	52.6	47.1	48.7
CIS	**35.3**	**34.7**	**34.9**	**35.8**
CEE	**51.6**	**50.3**	**49.6**	**49.3**
Turkey	42.6	44.3	45.3	46.4
Austria	**n.v.**	**n.v.**	**n.v.**	**n.v.**
Germany	n.v.	n.v.	n.v.	n.v.
Eurozone	**n.v.**	**n.v.**	**n.v.**	**n.v.**
USA	n.v.	n.v.	n.v.	n.v.

Source: Thomson Reuters, Raiffeisen RESEARCH

Exchange rate EUR/LCY (avg)

Countries	2011	2012	2013e	2014f
Poland	4.12	4.19	4.09	4.00
Hungary	279.3	289.2	297.5	290.0
Czech Rep.	24.6	25.1	25.3	24.5
Slovakia	euro	euro	euro	euro
Slovenia	euro	euro	euro	euro
Croatia	7.43	7.52	7.55	7.50
Bulgaria	1.96	1.96	1.96	1.96
Romania	4.24	4.46	4.37	4.38
Serbia	102.0	113.0	113.9	114.8
Bosnia a. H.	1.96	1.96	1.96	1.96
Albania	140.3	139.0	138.5	138.3
Russia	40.9	40.0	41.1	41.7
Ukraine	11.11	10.39	10.97	10.97
Belarus	6900	10700	12200	13700
Turkey	2.34	2.31	2.39	2.34
Austria	**euro**	**euro**	**euro**	**euro**
Germany	euro	euro	euro	euro
Eurozone	**euro**	**euro**	**euro**	**euro**
USA	1.39	1.29	1.33	1.33

Source: Thomson Reuters, Raiffeisen RESEARCH

Ratings[1]

Countries	S&P	Moody's	Fitch
Poland	A-	A2	A-
Hungary	BB	Ba1	BB+
Czech Rep.	AA-	A1	A+
Slovakia	A	A2	A+
Slovenia	A-	Ba1	BBB+
Croatia	BB+	Ba1	BBB-
Bulgaria	BBB	Baa2	BBB-
Romania	BB+	Baa3	BBB-
Serbia	BB-	not rated	BB-
Bosnia a. H.	B	B3	not rated
Albania	B+	B1	not rated
Russia	BBB	Baa1	BBB
Ukraine	B	B3	B
Belarus	B-	B3	not rated
Turkey	BB+	Baa3	BBB-
Austria	**AA+**	**Aaa**	**AAA**
Germany	AAA	Aaa	AAA
USA	AA+	Aaa	AAA

[1] for FCY, long-term debt
Source: Bloomberg, Raiffeisen RESEARCH

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