

Fitch affirms Croatia's rating

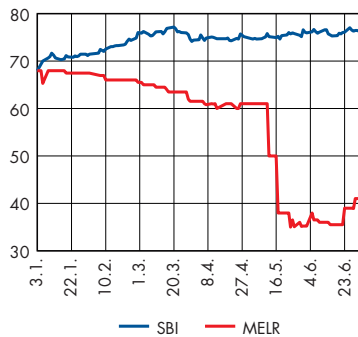
Croatia's ratings

Agency	Rating	Outlook	Last revision
Moody's	Ba2	Stable	10.3.2017
Fitch	BB	Stable	14.7.2017
S & P	BB	Stable	16.12.2016

* IT debt in FCY

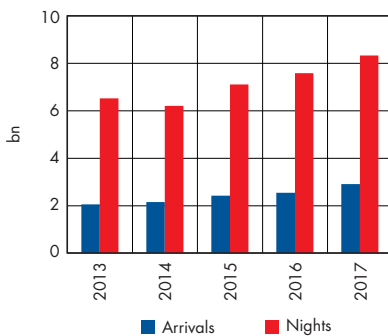
Sources: Eurostat, Economic RESEARCH/RBA

Mercator (ytd)



* as of 3rd July, 16:00 CET
Sources: Ljubljana Stock Exchange,
Economic RESEARCH/RBA

Tourist arrivals and nights, from Jan – May



Sources: CBS, Economic RESEARCH/RBA

In terms of data and news flow, the week was quite boring, which is not surprising considering the peak of tourist season and the fact that a majority of Croatia is on holidays or at least planning vacation. Also, Friday saw the last Parliament session before the summer break. Finally, Fitch changed neither the outlook nor the credit rating. Of course, agency expressed their concern regarding Agrokor and its impact on the overall economy. Fitch expects the Agrokor fallout will extend to the company's suppliers and banks and that it will impact employment, investment and credit growth, and cause real GDP growth to slow to 2.6% in 2017 in the event of an orderly restructuring.

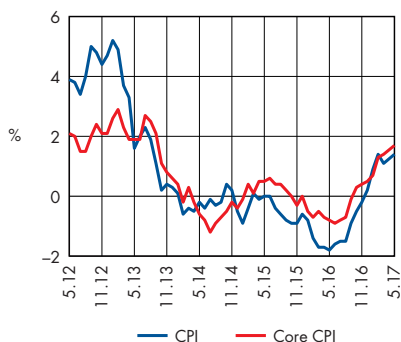
Therefore, all eyes remain on Agrokor and the peak tourist season.

In the meantime, we have not received any new official news regarding **Agrokor**, but the corporation's existence in its current form will probably not survive. When discussing the sale of some of the group's members, Ledo and Jamnica were always mentioned as the most likely targets. However, they are both burdened by joint guarantees for Agrokor's debt in the overall amount exceeding HRK 20bn. Accordingly, if Agrokor is unable to pay, the creditors have the right to seek payment from these companies. As the amount of guarantees issued likely exceeds the market capitalisation of these companies, their future will be determined by settlement with the creditors, which should be achieved in mid 2018 when the extraordinary administration is completed. As Mercator, the only one among the larger members of the group, is not burdened by guarantees, we think it is the most likely candidate for sale in the short run. The market capitalisation of Agrokor's share in Mercator as on 3 July 2017 was EUR 173.7 mn or 5% of Agrokor's financial debt. For the time being, the company announced only its intention to sell non-core companies, i.e. companies that do not belong to any of the strategic business branches of the corporation (retail, food production and agriculture).

Turning back to macroeconomics, as we have already written, in the period from January to May the number of **tourist arrivals** and **overnight** stays registered a solid growth (14.5% and 10% yoy, respectively). Of course, on average, a double-digit growth in 2017 seems unsustainable, but even an estimate at around 5% yoy growth of tourist overnights will definitely increase tourist receipts above EUR 9bn, thus contributing to the overall consumption and investment activity.

On Monday the CBS will release the **June CPI data**. We expect to see a slight deceleration on annual level (1% yoy), partially due to the fall in prices of telecommunications services. Still, modest but positive inflation is supported primarily by growth in the prices of food, beverages, transport, and prices in restaurants and hotels. In addition to the higher VAT on services in the hospitality industry, a share of the growth in the latter category is surely accounted for by a growing demand in tourism. On the other side, the rise in transport prices (almost entirely) and the annual growth in the category of food products were definitely aided by developments in the world's commodities markets. We expect energy prices to recover in the second part of the year (partly also due to the expiration of the

Inflation, average annual changes (%)



Sources: CNB, Economic RESEARCH/RBA

effect of administrative cuts in the prices of natural gas as of 1 April but also due to the already announced increase in electricity prices in H2 2017).

The very end of the week is reserved for the **May construction output** data and labour market statistics (the first estimate of May wages and the June unemployment rate). The first one is expected to continue with modest but positive annual growth rates suggesting rising investment activity partially supported by EU funds and very low base.

The **labour market** boasted a continued decline in unemployment, slow growth of employment and a growth in wages (gross wages above 3% and net wages around 5% yoy, whereas the tax reform from the begging of the year definitely drives the positive impact on net wages.)

Open market operations – CNB's FX interventions

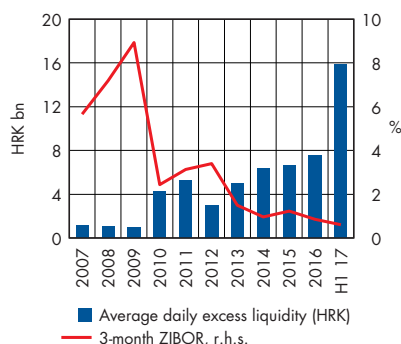


*until July 14th, Sources: CNB, Economic RESEARCH/RBA
Sources: CNB, Economic RESEARCH/RBA

Although the 2017 fall in unemployment started already in February, reaching its lowest levels of the past 20 odd years in April, the fact remains that the majority of the outflow from the unemployment register is a consequence of the so-called removal from the register due to non-adherence to statutory provisions and, to a smaller extent, due to new employment. In addition, new jobs are mostly seasonal jobs and/or jobs based on fixed-time employment contracts (mostly in trade and hospitality industry), while industry accounted for a smaller share of the employment growth. This means that the labour market remains fragile and burdened by serious structural problems of imbalance between supply and demand, long-term unemployment and fall in working-age population. Nevertheless, the **registered unemployment rate** in June will fall for the first time ever below 11%.

As for the financial markets, only Friday and the **FX intervention** brought some excitements. For the third time in 2017, the central bank intervened on the market by buying euros. Obviously, the FX intervention was not motivated by volatility of EUR/HRK. Namely, the majority of the last week's trading was held between 7.40 and 7.41 kuna per euro. Therefore, the latest CNB movement might be attributed once again to the expression of the CNB's readiness to keep its commitment to the policy of a stable EUR/HRK, which is the nominal anchor of the monetary policy in pursuing its objective (price stability).

HRK liquidity and MM interest rates



Sources: CNB, Economic RESEARCH/RBA

EUR/HRK might face further slight but persistent appreciation pressures as the main season is in full swing. But the CNB is keeping its eyes on FX volatility, and we have no doubt in its commitment to the HRK stability. Since the beginning of the year, the CNB has purchased EUR 476 mn directly from banks through the official FX interventions thus putting directly additional HRK liquidity (HRK 3.5 bn) on the market and for the same amount increasing FX reserves.

Market interest rates will consequently hold at their current low levels, possibly trending only slightly downwards but without any potential for growth until the end of the year. The average daily HRK liquidity surplus is still doubled in comparison with 2016, thus largely contributing to interest rates holding steady at low levels. Amid moderate inflation rates and stable EUR/HRK, the central bank is not expected to change the course of its policy. Moreover, its expansionary policy is likely to continue throughout the beginning of 2018.

Zrinka Živković Matijević, Ana Turudić

Atlantic Grupa sold two factories

Trading comment

The regular equity turnover on the Zagreb Stock Exchange last week amounted to HRK 4.7 mn daily on average. Thereof, the most traded were shares of Arena H.G. and preferred shares of Adris. Stock index CROBEX slid by 0.7% and shares of **Viadukt** lost the most (over 40%) among index members, following the release that the administrative settlement procedure of the company is terminated because the company filed for bankruptcy. Majority of equity indices in the region saw gains last week.

Company news

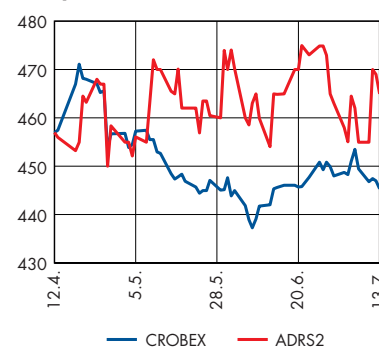
Atlantic Grupa sold its production facilities in Germany (Bleckede) and Croatia (Nova Gradiška) as well as private label business to a Belgium based company Aminolabs Group. Transaction amounts to near HRK 200 mn and does not include sale of brands Multipower, Champ and Multaben which remain in full ownership of the company. **AD Plastik** has been nominated for production of components for the vehicle Volvo V43X. The deal is worth EUR 22.8 mn in total sales over four years starting in April 2018. **Dalekovod** signed new contract worth over EUR 35 mn in Norway related to construction of 57 km long section of the transmission line. The state agency for restructuring and sale published its intention to sell up to 11.75% shares of **Luka Rijeka** in a block transaction after the public call for binding offers.

In this week

We expect a quiet week on the stock market ahead of Q2 2017 reporting season. Shares of tourism companies could continue to be in the focus of investors on the Zagreb Stock Exchange.

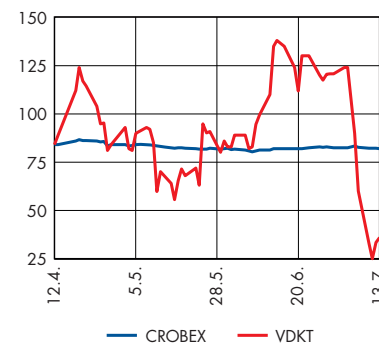
Nada Harambašić Nereau

Adris (p) (3 m)



Sources: ZSE, Economic RESEARCH/RBA

Viadukt (3 m)



Sources: ZSE, Economic RESEARCH/RBA

Market performance

Index	1w %	ytd %	Value on*
			14.7.2017
WIG30 (PL)	2.48	21.19	2,719
MICEX (RU)	2.37	-12.31	1,958
NTX (SEE,CE,EE)	2.06	20.25	1,217
ATX (AT)	1.68	21.34	3,177
SBI20 (SI)	1.37	13.22	812
BETI (RO)	1.19	14.89	8,140
BUX (HU)	0.99	12.04	35,857
PX (CZ)	0.78	8.50	1,000
BELEX15 (RS)	0.74	-0.32	715
SOFIX (BG)	0.73	21.60	713
CROBEX (HR)	-0.71	-6.83	1,859
SASX10 (BH)	-2.13	-10.71	617

* as at 16:30 CET.

Source: Bloomberg, Economic RESEARCH/RBA

Top/Flop – CROBEX index

Share	1w %	Price on*
		14.7.2017
Atlantska plovdba	3.88	401
AD Plastik	1.76	169
Dalekovod	1.61	23
Adris Grupa (P)	1.10	460
Atlantic Grupa	0.25	790
HT	0.12	180
Kraš	0.00	470
OT-Optima Telekom	0.00	3
Maistra	-0.07	299
Zagrebačka banka	-0.21	49
Zagrebačka burza	-0.29	14

* as at 16:30 CET.

Source: ZSE, Economic RESEARCH/RBA

Share	1w %	Price on*
		14.7.2017
Arenaturist	-0.35	480
Valamar Riviera	-0.71	44
Ingra	-2.89	4
Podravka	-3.14	315
Luka Ploče	-3.67	535
Končar – Elektroind.	-3.82	721
Uljanik plovdba	-4.40	130
Ericsson Nikola Tesla	-5.37	1,181
Đuro Đaković Grupa	-7.43	32
Petrokemija	-10.98	15
Viadukt	-41.78	35

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Abbreviations

bp – basis points	HBOR – Croatian Bank for Reconstruction and Development	Q1, Q2, Q3, Q4 – quarters
CERP – Restructuring and Sale Center	HNB – Croatian National Bank	RBA – Raiffeisenbank Austria d.d.
DPS – Dividend per share	IMF – International Monetary Fund	s.a. – seasonally adjusted
DZS – Croatian Bureau of Statistics	kn, HRK – Kuna	USD – Dollar
ECB – European Central Bank	MF – Ministry of Finance	WDA – working day adjusted
EUR – Euro	pp – percentage points	yoy – year-on-year
FED – Federal Reserve System		
GDP – Gross Domestic Product		

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% all IB services	0%	0%	0%	0%	0%	0%

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EU REGULATION NO 833/2014 CONCERNING RESTRICTIVE MEASURES IN VIEW OF RUSSIA'S ACTIONS DESTABILISING THE SITUATION IN UKRAINE

Please note that research is done and recommendations are given only in respect of financial instruments which are not affected by the sanctions under EU regulation no 833/2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine, as amended from time to time, i.e. financial instruments which have been issued before 1 August 2014.

We wish to call to your attention that the acquisition of financial instruments with a term exceeding 30 days issued after 31 July 2014 is prohibited under EU regulation no 833/2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine, as amended from time to time. No opinion is given with respect to such prohibited financial instruments.

INFORMATION REGARDING THE PRINCIPALITY OF LIECHTENSTEIN: COMMISSION DIRECTIVE 2003/125/EC of 22 December 2003 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards the fair presentation of investment recommendations and the disclosure of conflicts of interest has been incorporated into national law in the Principality of Liechtenstein by the Finanzanalyse-Marktmisbrauchs-Verordnung.

If any term of this Disclaimer is found to be illegal, invalid or unenforceable under any applicable law, such term shall, insofar as it is severable from the remaining terms, be deemed omitted from this Disclaimer. It shall in no way affect the legality, validity or enforceability of the remaining terms.