

rehabilitation that writes off or removes these assets and liabilities from the banking system or any debt-equity swaps that convert bank debt into equity in the enterprises. Information regarding such debt-equity swaps will be provided by the Ministry of Economy if and when they occur.

The above indicative limits will be cumulative and will be monitored on the basis of the average quarterly exchange rates (as listed in Annex III) from data collected monthly by the Ministry of Finance (ORESE) and supplied to the Fund within 30 days.

Statement by the IMF Staff Representative on the Republic of Croatia
February 3, 2003

This statement provides information that has become available since the issuance of the staff report on "Republic of Croatia—Request for Stand-By Arrangement." The new information does not change the thrust of the staff appraisal in that report.

1. As noted in the staff report on "Republic of Croatia—Request for Stand-By Arrangement," five prior actions remained to be completed before Board consideration of Croatia's stand-by request. On January 15, the Ministry of Finance provided consolidated budget data for the 53 largest local governments consistent with the fiscal program stipulated in the Memorandum of Economic and Financial Policies (MEFP). On January 17, the government opened three binding offers for 25 percent plus one share in the oil company (INA). On January 23, the government submitted to parliament a new budget law that satisfies the conditions specified in paragraph 16 of the MEFP and a labor law that satisfies the conditions specified in paragraph 24 of the MEFP. On January 24, the government issued a decree that limits the issuance of new guarantees to the amount by which old guarantees are amortized or expiring and reserves the right to issue guarantees to the Ministry of Finance. All prior actions have thus been completed.

2. Economic indicators suggest unexpected strength of economic activity. Real GDP grew by 6.5 percent year on year in the third quarter of 2002, bringing annual growth during the first nine months of the year to 5 percent. Investment and private consumption were particularly buoyant while external demand was weaker than expected. Retail sales volume recorded annual growth of 10.9 percent in November and industrial production grew by 8.1 percent year on year in December, raising its annual growth rate to 5.4 percent. Real GDP growth is thus likely to have exceeded the staff's projection of 4 percent in 2002.

3. The twelve-month rate of retail price inflation increased from 2.0 percent in November to 2.3 percent in December, while the core rate of inflation increased from 1 percent to 1.2 percent. On average, headline inflation fell from 4.9 percent in 2001 to 2.2 percent in 2002, while core inflation declined from 3.6 percent to 1.1 percent. On January 7, the CNB sold €75 million of foreign exchange to stem the seasonal depreciation of the kuna, which has remained stable against the euro since then.

4. The twelve-month rate of broad money growth continued to decelerate from 28 percent in September to 20 percent in November. However, the strong growth of bank credit to the private sector continued: while year-on-year growth of business lending declined from 22 percent in September to 21 percent in November, consumer credit accelerated further from 36 percent in September to 40 percent in November. Also, bank lending is increasingly being financed by foreign borrowing. In this situation, the CNB announced measures on January 15 to curb credit growth. Banks whose placements grow by more than 4 percent by end-March, 8 percent by end-June, 12 percent by end-September, and 16 percent by end-December 2003 will be obliged to buy CNB bills bearing interest of 0.5 percent for twice the amount of their excess credit expansion.