

# CHART OF THE WEEK

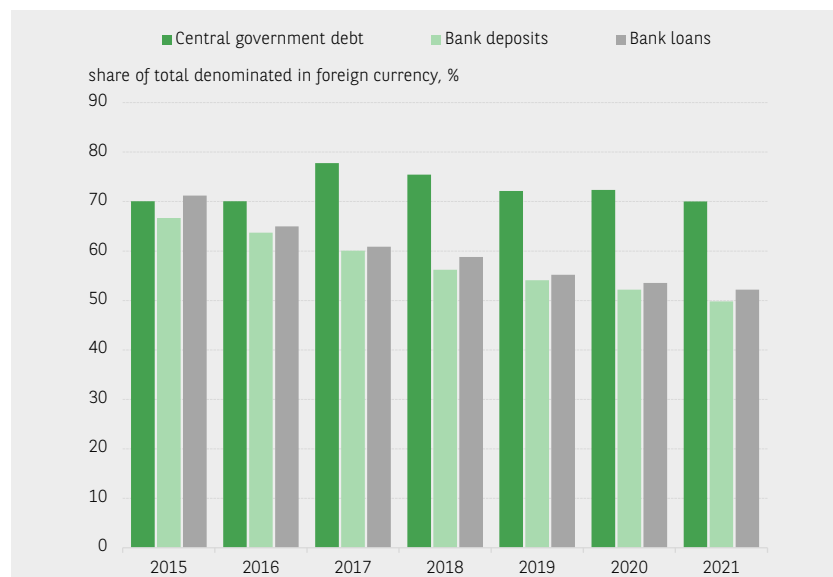


11 January 2023

## EURO ADOPTION STRENGTHENS CROATIA'S ECONOMY

Pascal Devaux

### Croatia: vulnerability to exchange risk



Source: BNC, BNP Paribas

On 1 January 2023, Croatia became the eurozone's twentieth member. By reducing foreign exchange risk, euro adoption significantly improves the country's macroeconomic solidity.

Through 2022, bank assets and government debt were largely denominated in foreign currency, mainly the euro. In this context, a sharp depreciation of the national currency could have systemic consequences and put entities holding foreign debt in a challenging financial situation.

Before adopting the euro, economic stability depended primarily on the central bank's capacity to maintain a fixed exchange rate between the Croatian kuna and the euro. Exchange rate stability was achieved via a high level of foreign reserves (equivalent to more than 10 months of imports of goods and services in 2022), bolstered by a current account surplus and European financial support (structural funds and a precautionary credit line from ECB).

Although recent years have been marked by a strong economic recovery (+10% in 2021) and healthier public and external accounts, the Croatian economy is still vulnerable. Economic growth and foreign currency inflows are highly dependent on the tourism sector, which contributes about a quarter of GDP and a third of current account revenues. Although foreign exchange risk has been reduced, the tourism sector's size as a share of the economy remains a non-negligible source of volatility.

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