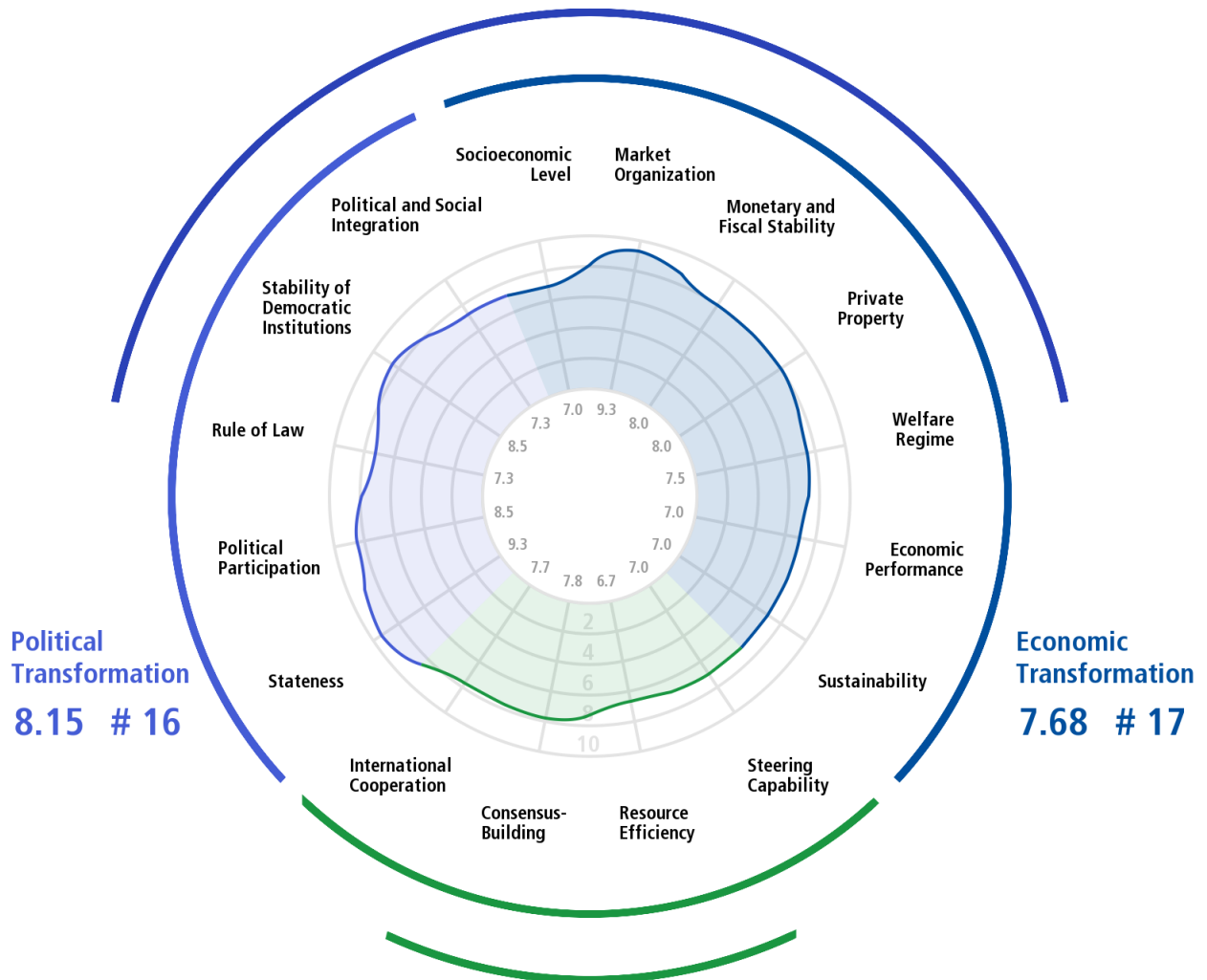


Croatia

Status Index

7.91 # 15

on 1-10 scale out of 137



Political Transformation
8.15 # 16

Economic Transformation
7.68 # 17

Governance Index

6.04 # 25

on 1-10 scale out of 137

This report is part of the **Bertelsmann Stiftung's Transformation Index (BTI) 2020**. It covers the period from February 1, 2017 to January 31, 2019. The BTI assesses the transformation toward democracy and a market economy as well as the quality of governance in 137 countries. More on the BTI at <https://www.bti-project.org>.

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Key Indicators

Population	M	4.1	HDI	0.837	GDP p.c., PPP \$	27505
Pop. growth ¹	% p.a.	-0.9	HDI rank of 189	46	Gini Index	31.1
Life expectancy	years	77.8	UN Education Index	0.796	Poverty ³	% 1.2
Urban population	%	56.9	Gender inequality ²	0.122	Aid per capita \$	-

Sources (as of December 2019): The World Bank, World Development Indicators 2019 | UNDP, Human Development Report 2019. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

Executive Summary

Early in its mandate, the HDZ-Most government, formed in October 2016, announced a series of reforms and introduced a rather substantial tax reform on January 1, 2017. At the same time, Croatia's largest company Agrokor almost went bankrupt. With more employees than any other company in Croatia and several other former Yugoslav countries, Agrokor has been a key actor in Croatia's export, food and agricultural industries. The Agrokor crisis posed a threat to numerous small agricultural producers and several large companies in Croatia, particularly in the food industry. The crisis also affected the Croatian government. In late April 2017, the HDZ-Most government collapsed after Most, the junior coalition partner, backed opposition demands for Finance Minister Zdravko Marić to resign due to a conflict of interest. Marić had previously been Agrokor's senior executive for strategy and capital markets. After Most ministers refused to vote against the no-confidence motion, Prime Minister Plenković sacked them. Despite the coalition government's collapse, political instability did not increase significantly and a third parliamentary election in three years was avoided. In July 2017, HDZ formed a new coalition government with HNS, previously a member of the center-left bloc led by the SDP. The formation of the new coalition government ensured a thin majority in every parliamentary vote throughout 2017 and 2018, with the government also supported by several small centrist parties and independent members of parliament.

GDP growth, which had resumed in 2015 for the first time since the six-year recession between 2009 and 2014, continued to increase in the period under review. Economic growth, however, was largely driven by the continued increase in household consumption rather than by a growth in net exports. Available export-import data for 2017 and 2018 indicates a slowing trend in the export of goods and services. Moreover, the 2013 to 2016 trend of increasing growth in exports relative to imports (6.2% compared to 5.1%) reversed in 2016, with the rate of import growth outpacing export growth. This new trend continued through 2017 and 2018. In addition, investment has increased steadily since 2015, although the rate of investment growth was lower in 2017 than in 2016. Due to these factors, GDP growth in Croatia was lower than in comparable Central and

Southeastern Europe countries during the review period. This is highlighted by the relatively low level of potential product in Croatia, which is still at 1.7% compared to 3.0% before the 2009 economic crisis. However, potential product growth will require substantial reform to public administration, the judiciary, the labor market, education and health care. During the review period, no such reforms were undertaken, except a partial education reform involving a pilot of a new curriculum. Meanwhile, economic reforms were limited to two relatively successful tax reforms, introduced at the beginning of 2017 and 2018.

History and Characteristics of Transformation

Croatia's transition toward democracy and a market economy has coincided with the disintegration of Yugoslavia and the armed conflicts arising from Yugoslavia's disintegration. As early as 1989, Croatia saw the beginning of an intensive process of political liberalization and forming of the first non-communist political parties. The dissolution of the League of Communists of Yugoslavia in January 1990 strengthened the mobilizing potential of the non-communist parties. The Croatian Democratic Union (HDZ), led by charismatic leader Franjo Tuđman, scored a convincing victory at the first multiparty election in Croatia in May 1990. The constitution of the Republic of Croatia was adopted at the end of 1990 and the referendum on independence was held in May 1991, with 93% of the Croatian population supporting Croatia's sovereignty and the possibility of joining a confederation of former Yugoslav republics. Following Serbian leader Slobodan Milošević's policy that all Serbs should live in Yugoslavia, the Serbs from the parts of Croatia where they constituted a majority or a dominant population rebelled against the Zagreb government. In mid-1991, the conflict escalated into open warfare. As the Yugoslav People's Army sided with the rebel Serbs, approximately one-third of Croatia's territory was occupied by the end of the first phase of the war in late 1991. The occupied territory stretched along a large part of the border with the neighboring Bosnia-Herzegovina and along the entire border with Serbia. The situation persisted until mid-1995, when Croatian troops liberated the occupied territories in the central and southern parts of the country. Most of the Serb population living in those parts left Croatia together with Serbian forces. As for the remaining occupied territories in Eastern Slavonia and Baranja along the border with Serbia, their peaceful reintegration into Croatia was successfully negotiated by the end of 1997. In addition to thousands of deaths, massive migration and widespread destruction, the war substantially slowed down the democratic transition and the development of democratic institutions. Although a democratic multiparty system was in place throughout the 1990s, in reality it was a semi-authoritarian form of political rule with President Franjo Tuđman and the ruling HDZ party dominating the politics on the national level. The opposition parties held power only at the local level, largely in the more developed western parts of the country and in some major cities. Popular opposition toward this political order started to grow in the late 1990s. After Tuđman's death, the center-left parties led by Social Democratic Party (SDP) and Croatian Social Liberal Party (HSL) won a large majority in the parliamentary election in early 2000. The ensuing political development started acquiring the fundamental characteristics of a democratic political rule, accompanied by a relatively intensive development of civil society organizations.

Unfortunately, it was also accompanied by a very high corruption rate reaching the highest levels of government. Nevertheless, Croatia experienced very strong economic growth between 2000 and 2008. The HDZ won the parliamentary elections in 2003 and then 2007, but this time with very pro-European leanings. In the mid-2009, prime minister and HDZ president Ivo Sanader (later charged with corruption) suddenly resigned, handing his mandate over to his deputy, Jadranka Kosor, who successfully completed the negotiations on Croatia's accession to the European Union. However, in the same the year, Croatia was hit hard by an economic crisis. For six years, neither the Kosor (HDZ) government nor the Milanović center-left coalition government led by SDP managed to pull the country out of the crisis. Despite Croatia's full membership in NATO in 2009 and accession to the European Union on 1 July 2013, the crisis persisted, accompanied by a growing emigration to other European countries. This emigration trend grew further through 2016 to 2019. Even the return to positive GDP growth in the second half of 2015 (the last year of the Milanović government), which continued under the Orešković and Plenković governments (2016 – 2019), did not stop the trend.

During the transition period, Croatia experienced not only a massive loss of population, but also considerable economic stagnation. In the early 1980s, as the western part of the socialist Yugoslavia, Croatia's GDP growth rate ranked among the highest of any socialist country, second only to Slovenia. Today, Croatia's GDP growth rate trails behind the former socialist countries of Central and Eastern Europe, now in the European Union. Croatia was hit hard by the 2009 economic crisis and, while economic growth had resumed by 2015, subsequent governments have failed to increase the competitiveness of the national economy.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The state has no rivals to its control over the country's territory. The police provides security for citizens and property across the entire territory of the state, and is administered by the central government, not by local or regional governments. This arrangement has been in place since 1995, when a Croatian army operation terminated the Republic of Serbian Krajina (established in 1991), incorporating the territory into the constitutional and legal order of the Republic of Croatia. The last part of the Republic of Serbian Krajina, the so-called District of Eastern Slavonia, Baranja and Western Sirmium, also established in late 1991, was peacefully integrated in 1998. That task was achieved on the basis of the Erdut agreement, signed in November of 1995 between the Croatian government and local Serbs.

The vast majority of the population agree that the nation-state is legitimate, and access to citizenship is equal to all individuals and groups without discrimination.

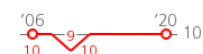
In March 2018, Milorad Pupovac, a deputy in the Croatian parliament and the president of the Serb National Council, warned of a deterioration in the status of Serbs in Croatia. Participating in a panel discussion at the Serb Cultural Society Prosvjeta in Sarajevo, he said that the status of Serbs in Croatia had deteriorated after Tomislav Karamarko took control of HDZ in 2012, with the party then in opposition. Karamarko turned HDZ, in Pupovac's opinion, into a strongly nationalistic party. Pupovac stated that the most important thing for the Serb community in Croatia is to prevent a further deterioration in the rights the community has gained.

There were attempts in 2018 to start a campaign that would limit the number of seats for ethnic Serbs in the Croatian parliament, as well as limit their influence on fiscal policy and government formation. This has, however, not resulted in any significant changes.

Question
Score

Monopoly on the
use of force

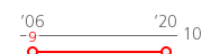
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_____ 1

State identity

9



_____ 1

In the period under review, the Catholic Church continued to engage in national and political topics, including direct involvement in political life. This is best exemplified by the church's involvement in the attempt to ratify the Istanbul Convention in parliament. The Catholic Church was strongly against adopting the document, claiming the document would usher in "gender ideology," considered by leading clergy as incompatible with the teachings of the church. However, the HDZ-led center-right government backed the adoption of the document, with Prime Minister Plenković a particularly strong supporter. In April 2018, 110 members of parliament voted to ratify the document, while 30 voted against and two abstained. Ten deputies from the ruling HDZ voted against ratifying the document, arguing that it would be unacceptable for HDZ, a party with Christian democratic values, to support such a document. In the end, the document was adopted with the votes of the majority of HDZ deputies and center-left deputies.

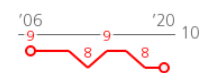
One important church-related political dispute has been the canonization of Archbishop Aloysius Stepinac, which was supported by the Catholic Church in Croatia and opposed by the Serbian Orthodox Church. The Serbian Orthodox Church tried to link Stepinac's activities with the Independent State of Croatia, a WWII Nazi puppet state and a direct protectorate of Germany and Italy, where numerous war crimes against the Serb population were committed. In the opinion of the Serbian Orthodox Church, Stepinac had not distance himself from the quisling regime, while the Catholic Church argued that he had condemned the regime and saved as many people as he could. This issue, as well as the churches' different interpretations of the 1991 to 1995 war, encumbers relations between the two churches, which remain strained, poor and full of mutual accusations.

Most basic civil functions of a state are provided throughout the country, but there are sharp differences in the quality of basic infrastructure and social service provision between developed urban areas and underdeveloped rural areas. A special administrative organization for tax administration within the Ministry of Finance is one of the most efficient governance bodies. Law enforcement is the responsibility of the police and several state agencies. The General Police Directorate (Ravnateljstvo policije) is responsible for the coordination of police activities and development of strategic police plans, while territorial tasks are the responsibility of the 21 police districts operating at the regional level. Law enforcement in the field of customs is in the hands of the Custom Administration, a separate branch within the Ministry of Finance. Inspection services are divided between several ministries. However, a centralized State Inspectorate is planned to be introduced in 2019 to overcome the fragmentation of responsibilities and the lack of coordination and policy coherence, which are seen as significant obstacles by the Plenković government.

Croatia has a highly developed motorway network, and relatively good connections between the islands and the mainland, although the train network is underdeveloped.

No interference of religious dogmas

8



1

Basic administration

10



1

Transport connections (bus and rail) in less developed and rural areas are poor. In comparison to other EU member states, Croatia's achievements in the digitalization of service delivery are modest, but the introduction of a e-citizen platform in 2014 represented a substantial improvement. There are sharp differences in social service provision between developed and underdeveloped regions. In particular, basic health care services are insufficient in remote rural areas and on the islands. More than 87% of Croatian population use public water supplies and drink tap water, which is regularly monitored for health and safety standards.

The state administrative structure covers the entire territory. It consists of 20 ministries, five government offices, seven state administrative organizations and 20 state administration offices in the counties. 1,279 local units of the central state administration bodies and local offices conduct central state administration affairs in counties, cities and communes. Also, a total of 91 local offices and 302 registrar's offices have been established in communes and cities for conducting county state administration affairs. In addition, there are numerous other public bodies, an extended structure of 555 local self-government units (127 cities and 428 communes) and a regional self-government structure of 20 counties.

2 | Political Participation

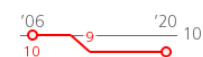
The legal framework of political-party and electoral-campaign financing is well-structured, but the enforcement of legal provisions and effective legal sanctioning of violations of law is weak due to the rather low capacities of the State Electoral Commission as the central body in charge of monitoring political financing.

Parliamentary elections are based on proportional representation (PR) and seats are distributed according to the D'Hondt system. From 2015, parliamentary elections voters can vote for a party list or for a specific candidate. The personalized element of voting was introduced as a result of a campaign by some small groups and parties to introduce voting for a candidate and not for a party list. A majoritarian system was not accepted by the ruling coalition and instead preferential voting was introduced in a PR system. Croatia has 10 electoral districts, each electing 14 members of parliament. The eight remaining members of parliament are elected by national minorities (with three seats reserved for the Serb minority). Three additional members of parliament are elected by Croatian citizens with no permanent residence in Croatia (the diaspora).

Although elections are carried out in accordance with basic democratic standards, ever since the introduction of PR, variation in size of electoral districts has been a problem. Pursuant to electoral law, the number of voters in an electoral district should not exceed 5% of the average number of voters in an electoral district. In all parliamentary elections held under the current system since 2000, there were departures from the law. While initially the difference exceeded 5% in three districts,

Free and fair elections

9



1

in the two last elections (in 2015 and 2016), it happened in all but two districts. Such departures have affected the numbers of seats won by individual parties. Therefore, ensuring the appropriate size of electoral districts has become a key topic in discussions on electoral reform.

The democratically elected representatives possess an effective power to govern. While some interest groups have significant influence, it does not limit the power to govern. As the social partnership system in place in Croatia is only partially efficient, strong groups such as the most powerful entrepreneurs (who usually have a direct influence on government decisions, not through the social partnership), war veterans and representatives of the Catholic Church exercise influence over many important political decisions behind the scenes. They can occasionally force the government's hand on special interest policies. The Catholic Church and associated groups have influenced government decisions on women's and LGBT rights. In November 2014, veterans of the 1991 to 1995 war raised a large tent in downtown Zagreb in political defiance to the then center-left government of Prime Minister Milanović and President Josipović. The tent was removed only in April 2016, after the new center-right HDZ-MOST coalition had come to power on all levels. War veterans have also been influential in campaigning to limit Serb minority rights.

For years, those with the requisite hidden power to block government efforts were people from the business community. In public opinion, prominent members of the business community, such as powerful Croatian entrepreneur Ivica Todorić, held positions typical of a veto player and were capable of blocking government efforts that were not to their advantage. The financial collapse of Todorić's company, Agrokor, in the early 2017 forced the government to pass the Act on Compulsory Administration Procedure in Companies of Systemic Importance for the Republic of Croatia, which was directed primarily against Agrokor – hence its popular name Lex Agrokor. Based on this law, a special commissioner was appointed for the company and, in 2018, a new ownership structure was approved by the creditors' council, depriving Todorić of ownership. Thus, even the most powerful members of Croatia's business community, hitherto believed to be able to block the decisions of legitimate authorities, can be subdued to these decisions.

Croatian citizens face no limitations when organizing political or civil initiatives. Freedom of association has been an unquestionable achievement of the democratic development of Croatia. There is a rather strong network of civil society organizations in Croatia.

However, civil society organizations are restricted when they are perceived to be challenging nation- and state-building projects in Croatia. While civil society groups have extensive legal protections, funding is used to favor the policy impact of certain groups over others. For example, war veterans' associations and groups associated with the Catholic Church receive preferential treatment, increased funding and media

Effective power to govern

9



1

Association / assembly rights

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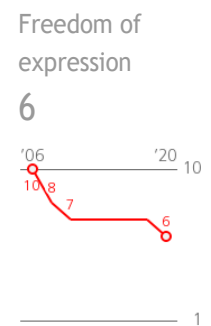
coverage. This is often to the detriment of human rights and minority rights NGOs, who are seen as opposing the foundations of the Croatian state and nation.

In recent years, conservative NGOs have become more prominent. They gathered momentum during the center-left government of Zoran Milanović (2011 – 2015) and President Ivo Josipović (2010 – 2015), elected as a candidate from the left. Previously, mostly NGOs advocating liberal-left values were active in the public scene. The civic initiatives “People’s Choice,” which campaigned for a referendum on electoral reform, and “Truth about the Declaration of Istanbul,” which campaigned against the Declaration of Istanbul adopted by the Croatian parliament in April 2018, attracted particular attention during the review period. Various war veterans’ organizations featured prominently among those who advocated national values.

Freedom of expression is constitutionally guaranteed, but occasionally subject to interference. Croatian Radiotelevision (HRT) not only functions as a public broadcasting company, but also promotes the political issues convenient to the incumbent government. This was evident in 2016 when, after the center-right parties had won the parliamentary elections, the influence of conservative-right political commentators grew substantially. In March 2016, the Orešković government replaced the head of HRT with an adviser to HDZ President Tomislav Karamarko who subsequently dismissed about 70 TV directors, editors, journalists and staff members. In 2018, various NGOs strongly criticized the continued politicization of HRT and pressure exerted on HRT journalists. The criticism was provoked by the resignation of Hrvoje Zovko, a TV journalist and program editor, on account of the censorship and external pressure on his editorial policy he had faced.

The other example of the violation of freedom of expression involved the Croatian Audiovisual Center (HAVC). Since influential associations of veterans criticized HAVC for supporting a documentary about the killing of disabled Serbian civilians at the end of the 1995 war, the Orešković government and its right-wing extremist minister of culture launched an investigation into HAVC. Eventually, in early 2017, the director of HAVC was accused of authorizing illegal financial transactions and replaced, despite the support of the majority of leading filmmakers in Croatia.

Court proceedings represent a third problem. In early 2019, the Croatian Journalists Association announced there were more than 1,000 ongoing court proceedings against journalists and media outlets. Not only have there been numerous cases in which judgments have favored local elites and their family members over local media, but a number of absurd court rulings have attracted national attention. For example, in the late 2018, a satirical website was found guilty of publishing lies about a radical right-wing TV journalist, although the content was satirical. Other examples demonstrate that court decisions threaten freedom of expression. One of the most striking examples was the January 2019 ruling against Jurica Pavičić, the Split-based acclaimed columnist, writer and film critic. The former Split theater manager Duško Mucalo sued Pavičić for a number of articles about Mucalo’s incompetence in



managing the cultural institution. Mucalo claimed he “felt ashamed” because of the criticism. Pavičić was fined HRK 50,000 (€6,600) – approximately eight times the average monthly salary in Croatia.

3 | Rule of Law

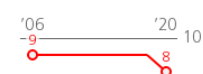
The executive in Croatia has substantial powers, while the parliament merely performs a supervisory function. However, the parliament has performed this function poorly and is perceived by the public as the country’s weakest political institution. Attempts to strengthen the parliament’s supervisory role through investigative parliamentary committees and interpellations have had limited success. This was obvious in the case of the investigative parliamentary committee into the causes of the collapse of Agrokor, Croatia’s largest company. It was expected that the committee would shed light on the roles of all the significant actors in Agrokor’s collapse. However, after the State Attorney’s Office launched an investigation of key company personnel, the ruling HDZ party terminated the committee’s activities. This showed that existing instruments for public participation in parliamentary work are poorly used in Croatia.

Early in President Kolinda Grabar-Kitarović’s term in office, it was publicly discussed that the constitutional position of the president of the republic should be extended – specifically, concerning the appointment of foreign and defense ministers. The proposed idea was for the president to be entitled to give consent to the government’s appointments for these roles. However, the idea was abandoned.

The number of judges and court personnel per capita in Croatia is among the highest in Europe. Yet, Croatia’s judicial system is one of the least efficient in the European Union. As part of Croatia’s EU accession process, substantial changes were made to the procedures for appointing members of the State Judicial Council and electing judges. The Milanović government (2011 – 2015) introduced a series of judicial reforms. In early 2013, the government changed the process by which high court (i.e., Supreme Court, High Commercial Court, High Misdemeanor Court and High Administrative Courts) justices were appointed. In addition to the seven judges that represent the various courts, this group now also includes two representatives of law schools and two parliamentary appointees. In 2014 and 2015, the government succeeded in substantially reducing the number of courts and in overhauling misdemeanor legislation. Under the Milanović government, the number of misdemeanors has fallen. In 2018, the Plenković government made several minor changes to the justice system, which the justice minister called a “mini reform.” Apart from joining misdemeanors and municipal courts, the mini reform prescribed shorter deadlines, provided provisions to speed up and reduce political interference in the appointment of judges. Consequently, the justice minister will no longer be able to appoint individual judges. The mini reform also introduced clearer procedures for the

Separation of powers

8



1

Independent judiciary

7



1

election of the president of the Supreme Court and the chief state attorney. However, judicial inefficiency, the long duration of cases, the low level of digitalization and the extremely high level of corruption remain systemic problems.

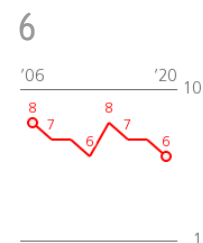
Although an institutional framework for the election of judges has been created, the public still has a negative perception of the independence of the judiciary. According to the 2018 EU Justice Scoreboard, only 23% of Croatian citizens believe that the country's judiciary is independent. This places Croatia behind all other EU member states, despite the fact that it ranked fourth in the European Union in terms of the per capita budget allocated to the judiciary and first in terms of the number of judges per 100,000 inhabitants in 2016. Marin Mrčela, an acclaimed Croatian judge and president of GRECO (the Group of States against Corruption), believes that public perception of judicial independence is undermined by the government's failure to implement an important GRECO recommendation (an improvement to the quality of the judiciary's communication with the public, which would present the good and bad sides of the judiciary more transparently). Further reasons for the public perception include the length of court proceedings, and the very small number of successful prosecutions of politicians, well-known public personalities and people in important positions.

The crucial problem in successfully prosecuting officeholders who abuse their positions is the limited number of final verdicts against senior officials, against whom indictments have been raised by the State Attorney's Office or the State's Office for the Suppression of Organized Crime and Corruption (USKOK). For instance, five indictments were raised against former prime minister Ivo Sanader and he was accused of stealing more than HRK 100 million in public money. After Sanader was arrested in mid-2011 and following several years in court proceedings, the Croatian judiciary failed to issue a final verdict against him. As many as three first-instance convictions against Sanader were dropped at the Supreme Court or reversed by the Constitutional Court.

In 2018, it was formally established that the Minister of Economy Martina Dalić and Minister of Finance Zdravko Marić had violated conflict of interest disclosure rules related to the state bailout of food conglomerate Agrokor. However, the ruling did not impose any penalties on the two ministers, although Dalić resigned in the wake of the scandal, while still denying any wrongdoing. Milan Bandić, who was elected mayor of Zagreb for a sixth term in 2017, has faced constant accusations of corruption and abuse of office, and has once been arrested. However, Bandić has so far always been acquitted.

Corruption is particularly prevalent in the judicial system, numerous business and non-businesspeople have indicated that irregular payments and bribes are solicited for favorable judicial decisions. Confidence in judicial independence is extremely

Prosecution of
office abuse



low. This is also due to lengthy court proceedings, potential political interference and bias in court decisions.

Corruption in the public procurement system is also high. More than 60% of businesses believe that corruption is widespread in public procurement, both at the national and local levels. Corruption in the provision of public services is perceived to be moderate. According to international reports, one in six companies expect to give gifts to public officials in order to get things done, while four out of five business executives confirm that bribery and corrupt practices are widespread in the businesses sector. A particular problem in public service provision is the prevalence of clientelism and party patronage in public administration recruitment processes, which severely curtails government efficiency. As a result, bureaucracy in Croatia is relatively inefficient at both the national and local government levels by EU standards – a situation that is further exacerbated by low regulatory transparency. It is estimated that corruption has reduced Croatia’s GDP rate by about 15%.

Croatia’s independent media and NGOs contribute slightly to a reduction in corruption by focusing public attention on severe cases, especially cases involving senior public officials. However, the absence of structural reforms in public administration and the judicial system substantially limit such efforts.

In their reports in 2017 and 2018, a number of NGOs pointed out that the protection of human rights in Croatia, while formally in place, is still not satisfactory. In the opinion of the NGOs, one of the key reasons for this is the fact that the protection of human rights is still not among governments’ top priorities. According to the NGOs, the fact that the new National Program of Protection and Promotion of Human Rights has still not been adopted, although the old program expired in late 2016, is evidence of this.

LGBT, women’s, minority and human rights, although usually legally enshrined, are not consistently respected or protected. There have been gradual, but consistent, moves to erode some of these rights. For example, the Istanbul Convention was not ratified; there have been calls to limit minority language rights in certain cities and minority voting rights in parliament; and the constitution was changed to restrict marriage to a union between a man and a woman. (However, from 2014, “life partnership” grants same-sex couples the same rights, excluding the right to adopt, as married couples). Domestic violence remains a problem. While this is being actively tackled by civil society organizations and media outlets, it remains difficult to prosecute domestic violence through the judicial system.

Civil rights

8



1

4 | Stability of Democratic Institutions

Democratic institutions are relatively stable and face no significant problems in performing their basic tasks. After the state-building process was completed in the mid-1990s, the Croatian political system achieved a higher level of institutionalization and moderate party pluralism. This was especially apparent after 2000 when the left-center coalition of political parties defeated the dominant HDZ (Croatian Democratic Union). After 2005 and the beginning of EU accession negotiations, Europeanization has had a strong impact on the institutionalization of the Croatian political system.

There is a clear division of powers between different levels of government (state, regional and local), and between the executive, legislature and judiciary. The activities of independent control agencies, which were largely established as a part of the Europeanization process, substantially contributed to the stability of democratic institutions by increasing public accountability. These agencies include the Commission for Conflict of Interest (set up in 2011) and the Commissioner for Information (2013), which is an independent body for the protection of the citizens' right of access to information. The commissioner's office has developed several channels to make information publicly available.

The stability of democratic institutions has been threatened by two parallel processes. First, there is a growing influence of populist movements organizing public campaigns and referendums. Such movements not only partake in such actions, they also challenge the democratically elected government and demand the resignation of ministers who oppose their views. For example, war veterans protested against a minister of the Milanović government in charge of the Ministry of War Veterans. The protests had begun in 2014 with pitching a tent in front of the ministry. The tent was not removed until April 2016, after both the center-left president Ivo Josipović and the center-left coalition government led by SDP had lost power. In 2018, conservative NGOs submitted to the parliament a petition signed by more than 400,000 people supporting a referendum against minority rights and a petition with over 340,000 signatures rejecting the Istanbul Convention (adopted by the parliament in April 2018).

Performance of democratic institutions

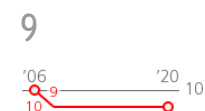
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A large majority of relevant political actors (e.g., central and local government bodies, political parties, business associations, trade unions and civil society organizations) accept the fundamental democratic institutions of the Republic of Croatia. An exception to this are some minor and marginal extreme-right political parties that glorify the Ustasha's fascist Independent State of Croatia, which existed from 1941 to 1945. Their influence on the political process is almost negligible, but their activities do present a problem. Many right-wing politicians and a part of the society have covertly glorified the Independent State of Croatia at public events. It is expressed in radical nationalist speeches and by using Ustasha's iconography. Although the Ustasha ideology is officially condemned, a part of society and the political elite, including some members of the governing party HDZ, have not accepted all liberal democratic values.

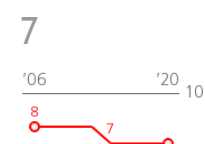
Commitment to democratic institutions



5 | Political and Social Integration

The decline of SDP – which followed the party's narrow defeat and loss of power in the 2015 parliamentary elections, and further defeat in the 2016 parliamentary elections – marked a substantial change in Croatian politics. The striking decline of SDP, whose political support was reduced by practically half, led to the fragmentation of the center-left bloc. The significance of the rivalry between HDZ and SDP declined, and HDZ emerged dominant, as the center-right and centrist parties rallied behind HDZ. The populist Human Shield (Živi zid) has become the third most popular party in opinion polls, almost reaching the levels of SDP. The right-wing Bridge (Most) ranks fourth and has established strong ties with the conservative NGOs that launched two referendum initiatives in 2018. These are the only four political parties that regularly exceed 5% in opinion polls. In addition, the center-left Amsterdam Coalition of six parties can count on crossing the 5% electoral threshold. The Bandić Milan 365 – Labor and Solidarity Party, led by Zagreb mayor Milan Bandić, won one parliamentary seat in the last election in 2016. Nevertheless, by early 2019, the party had 10 members of parliament, as ethnic minority deputies and defectors from other parties joined Bandić's party. Consequently, Bandić's party now has more seats in parliament than the Croatian People's Party – Liberal Democrats (HNS), HDZ's main coalition partner.

Party system



In Croatia, there is a completely institutionalized system supporting the involvement of interest groups in the policy-making process. There is also a completely formalized system of social partnership that consists of governments, employers' associations and trade union organizations. In 2009, parliament enacted a Code of Practice on Consultation with the interested public in the process of adopting laws, other regulations and policies, which opened additional space for interest groups to be involved in policy-making process. However, government has retained authoritative decision-making powers. But that does not mean that the power of interest groups is generally small and significant differences in the degree of influence on politics

Interest groups



between various interest groups do not exist. There are relatively strong bipartite arrangements between government and various business associations. These arrangements include regular contact between representatives of employers' associations, representatives of banks and members of government, as well as a series of hidden influences, mostly nontransparent and out of sight of the public. This is especially true of the largest entrepreneurs in Croatia. Compared with the power of entrepreneurs, the power of trade unions is much lower. The number of trade union members was drastically reduced since independence in 1991. The influence of trade unions is stronger in the public than in the private sector. Beside this, there are very strong arrangements with individual advocacy groups, which are often marked by some form of clientelism. This is especially true in the case of war veterans and policies that apply to them. Various professional associations have an extremely large impact on governance, such as associations of doctors, lawyers or similar professions. They are often able to block important government policies.

Popular satisfaction with the functioning of democracy in Croatia remains very low. According to the Eurobarometer report published in autumn 2017, only 27% of citizens are satisfied, while 72% are not satisfied with the functioning of democracy in Croatia – the second worst score among EU member states and well below the EU average of 56% satisfied and 42% not satisfied.

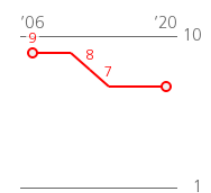
The European Quality of Life Survey showed that Croatia has the lowest trust in political institutions in the European Union, scoring on average 3.8 on a scale from 1 (“do not trust at all”) to 10 (“trust completely”). However, the level of trust increased in 2016 compared to the 2011 survey.

The Barometer of Croatian Society (Ivo Pilar Institute, Zagreb) showed that the most trusted public institution is the Croatian army. In the 2016 survey, the military scored 5.67 (on a scale of 0 – 10), followed by educational institutions (5.59) and health care (5.21). The Catholic Church (4.94), the president (4.67), the police (4.42) and the European Parliament (3.82) have medium levels of trust, while the judiciary (3.14), the government (3.12), the Croatian parliament (2.86) and Croatian political parties (2.49) rank lowest.

The lack of public trust in political institutions is reflected in very low electoral turnout. In the last three parliamentary elections, turnout never exceeded 70% and fell below 60% in 2016. This constitutes a strong downward trend compared to the 2000 parliamentary elections when turnout was 76.5%. Turnout at local elections is usually even lower, seldom reaching 50%.

Approval of
democracy

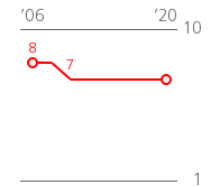
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As an analytical construct, social capital has various dimensions that define it, including social and political trust, participation in decision-making, and civic philosophy. Research carried out by Croatian social scientists suggests that Croatian citizens constitute the most important variable that a crucial social capital-related problem concerns its regional distribution, as there are substantial differences in the distribution of social capital between Croatian regions. According to the European Quality of Life Survey 2016, Croatia had the second lowest level of interpersonal trust in the European Union (only above Cyprus), while civic engagement levels have declined since the 2013 survey.

Social capital

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II. Economic Transformation

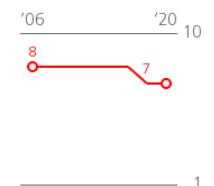
6 | Level of Socioeconomic Development

Croatia has considerably higher levels of human development than the rest of the Western Balkans apart from Slovenia. The poverty level is very modest (1.2% in 2015) and gender inequality is among the lowest in the region.

The Gini coefficient places Croatia among countries with moderate inequality, although there are significant regional disparities. Croatia is divided into 20 counties and the City of Zagreb. Only the GDP of Zagreb exceeds the EU average (approximately 103%). Only two Croatian counties – Istria and Primorje-Gorski Kotar, both in western Croatia – have reached almost 75% of the EU average. Dubrovnik-Neretva has reached about 60% of the EU average. All other counties are far below this level. The situation is most acute in Slavonia where four of the region's five counties rank as the poorest counties in Croatia (with GDP a mere one-third of the average EU GDP). In Slavonia, only Osijek-Baranja county – which includes Osijek, the largest city in eastern Croatia – has a somewhat higher GDP. Neither the policies of the Croatian government nor six years of EU membership and access to EU's cohesion policy measures have stopped the socioeconomic slide of a region that was rather developed during the period of socialist modernization. Today, it is facing a high level of emigration and various aspects of socioeconomic regression.

Question
ScoreSocioeconomic
barriers

7



Economic indicators		2015	2016	2017	2018
GDP	\$ M	49519.0	51623.4	55201.4	60805.7
GDP growth	%	2.4	3.5	2.9	2.6
Inflation (CPI)	%	-0.5	-1.1	1.1	1.5
Unemployment	%	16.2	13.1	11.2	8.9
Foreign direct investment	% of GDP	0.3	3.6	3.7	2.1
Export growth	%	9.4	5.6	6.4	2.8
Import growth	%	9.2	6.2	8.1	5.5
Current account balance	\$ M	2491.6	1389.9	2997.5	1459.0

Economic indicators		2015	2016	2017	2018
Public debt	% of GDP	83.7	80.5	77.8	74.6
External debt	\$ M	-	-	-	-
Total debt service	\$ M	-	-	-	-
Net lending/borrowing	% of GDP	-3.5	-0.9	0.9	-
Tax revenue	% of GDP	20.8	21.4	21.6	-
Government consumption	% of GDP	19.9	19.4	19.5	19.7
Public education spending	% of GDP	-	-	-	-
Public health spending	% of GDP	5.6	5.6	-	-
R&D expenditure	% of GDP	0.8	0.9	0.9	-
Military expenditure	% of GDP	1.5	1.4	1.4	1.5

Sources (as of December 2019): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

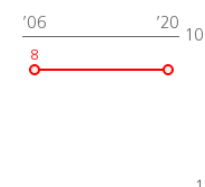
Although there are no formal barriers to production factor mobility (labor, capital) or any other limitations in the product and service markets, weak institutions undermine the entrepreneurial climate. According to a report by the Croatian Employers' Association (HUP) published in late 2018, Croatia lacks the capacity for rapid economic growth and convergence. The report is part of a regular analysis of Croatia's reform implementation capacity across 12 basic areas, which has been carried out by HUP since Croatia's accession to the European Union in 2013. The report analyzes a long list of indicators, which in the employers' opinion slightly deteriorated between 2017 and 2018. One of the biggest deteriorations concerned investment and business barriers, which is reflected in the number of procedures required for starting a business, building permit fees and local rates to be paid by investors. Negative trends were also recorded in the evaluation of the entrepreneurial climate and investment growth. These negative findings were echoed in the World Bank's 2019 Ease of Doing Business Index in which Croatia ranked 58 out of 190 countries, compared to rank 40 in 2016. Establishing a business is particularly difficult in Croatia, as it takes eight procedures and 22.5 days, and costs 6.6% of GNI per capita, ranking the country 123 out of 190 countries for the sub-index "starting a business."

As Croatia is a member of the European Union, Croatia's competition policy follows strict EU rules. The Croatian Competition Agency consistently implements the community law in this area, functioning like an implementing body of the European Union. The biggest challenge in this area during the review period was the financial crisis that almost bankrupted Uljanik shipyard in Pula and Treći maj shipyard in Rijeka in the second half of 2018. The Croatian government tried to help these shipyards recover financial soundness, but government subsidies to the shipyards had to be negotiated with the European Commission.

The Croatian government is implementing the EU competition policy fully in line with the European Commission's market competition rules. In January 2018, acting in line with EU rules on state aid, the European Commission approved a state guarantee for a €96 million loan to Uljanik. In September 2018, the European Commissioner met with the president of the Croatian government, whereby it was agreed that the attempt to restructure the Uljanik shipyard in Pula and Rijeka (which includes two of the three largest Croatian shipyards) would be fully implemented in accordance with EU rules, and must respect market competition, save taxpayers' money and involve contributions by market stakeholders.

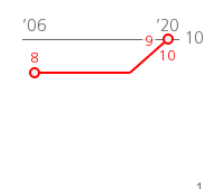
Market organization

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Competition policy

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When Croatia joined the European Union in 2013, its market became part of the European single market. This led to a large increase in international trade and in the number of companies participating in the Croatian economy. The number of Croatian companies trading with the EU market increased from 4,096 in 2013 to 6,323 in 2017. This led to a substantial increase in the share of exports and imports in Croatia's GDP. In particular, a substantial increase in exports was recorded.

Liberalization of foreign trade

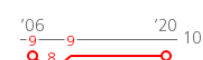
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Even before a financial crisis affected Croatia's largest company Agrokor in early 2017, the Croatian central bank tried to ensure the timely and consistent implementation of prudential regulation, and limit Croatian banks' exposure to Agrokor. The stability of Croatia's financial system was maintained and the sector was not substantially negatively affected by the crisis. Interest rates have continued to decline. In 2017, the average interest rate was 3.9%, compared to 5.7% in 2012, immediately before Croatia's accession to the European Union.

Banking system

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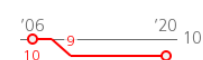
The Croatian banking system is relatively stable and has a high level of liquidity. All key banks in Croatia are foreign owned. The largest domestic-owned bank, the Croatian Postal Bank (HPB), controls about 5% of total banking sector assets. The share of non-performing loans in Croatia is slightly above the EU average and similar to neighboring EU member states (11.7% in 2018). However, the capital adequacy ratio is above the EU average (20% in Croatia compared to an EU average of 18%), according to the European Commission's 2018 Convergence Report.

8 | Monetary and fiscal stability

During the review period, the average annual inflation rate went up from 1.1% in 2017 to 1.5% in 2018. The kuna to euro exchange rate averaged HRK 7.46 to €1 in 2017 and decreased to HRK 7.41 to €1 in 2018. The appreciation in the value of the kuna was largely due to favorable macroeconomic trends, including reduced fiscal risks and the relatively stable economic recovery (GDP has continuously increased since 2015). The Croatian central bank continued to implement an independent monetary policy, with stability of the kuna to euro exchange rate the nominal anchor of the policy. The central bank has pursued an expansive monetary policy, while supporting high liquidity in the monetary system. Because of the appreciation pressure on the kuna, the central bank bought substantial amounts of foreign currency from commercial banks, increasing the overall supply of local currency.

Monetary stability

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In cooperation with the government, the central bank developed and presented the Strategy for the Adoption of the Euro. Regardless of the fact that most citizens are against the adoption of the euro, the central bank strongly supports Croatia's accession to the European Monetary Union. The central bank believes that the benefits of adopting the euro will be lasting and exceed the related costs, which the

central bank argues will be low and temporary. One of the reasons why the adoption of the euro could be favorable to Croatia is the fact that more than 80% of savings, and 70% of the liabilities of Croatian legal and physical entities are in euros. Consequently, the Croatian economy is very exposed to exchange rate risks. It is believed that the adoption of the euro would eliminate exchange rate risks for citizens, companies and the state, while also reducing interest rates and stimulating investment.

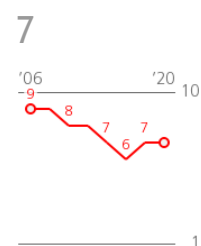
In the first half of 2017, owing to a rather strong fiscal adjustment carried out in 2015 and 2016, Croatia exited the Excessive Deficit Procedure. Favorable trends in public finances continued in 2017 and 2018, recording for the first time a consolidated general government budget surplus of HRK 3.4 billion. Such trends were primarily influenced by vibrant economic activity, an increase in tax revenue and a decrease in interest rate expenditure. As a result, not even measures in the opposite direction (e.g., a substantial reduction in personal income tax) jeopardized the stability of public finances and the fundamental goals of the fiscal policy. These trends led to a reduction in public debt, which had grown significantly since the beginning of the economic crisis in 2009. Public debt had peaked in 2014 and 2015, reaching approximately 85% of GDP. A downward trend in public debt then ensued, which continued through the period review. In early 2019, public debt equaled 75% of GDP. The stability of fiscal policy could lead to an increase in Croatia's credit rating and ensure access to cheaper government financing.

9 | Private Property

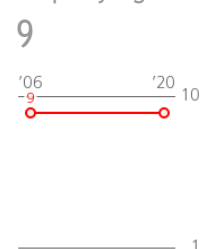
Property rights and regulations on acquisition, benefits, use and sale of property are well defined. The right to ownership of private property is established in the Croatian constitution and in several laws and regulations. During the negotiation process for EU membership, Croatia agreed to a seven-year transition period during which nationals from other EU member states would not be entitled to purchase agricultural land in Croatia. The protection of property rights is one of the best evaluated components of competitiveness in Croatia, according to the World Bank's Doing Business Report 2017 to 2018.

Property tax, which is a standard policy tool in most European countries, has never been introduced in Croatia. Although the Ministry of Finance and local government units started work on a legal proposal to introduce a property tax, Prime Minister Andrej Plenković promised to postpone the introduction of property tax in August 2017. His reaction was caused by the negative statements expressed by a large number of citizens, NGOs and some political parties. The proposal has been labelled an extra burden on citizens, with as many as 90% of Croatian citizens owning real estate, the highest rate among EU member states. The Croatian government decided to postpone the introduction of a property tax, despite the fact that property taxes are

Fiscal stability



Property rights



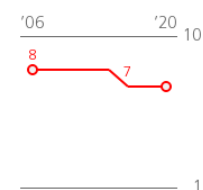
part of the policy measures recommended by the European Commission, within the European semester procedure, and irrespective of the fact that several leading economists have suggested that the introduction of a property tax would stimulate further development of the property market. Nevertheless, opponents of the new tax stressed the inappropriateness of the tax in a country where citizens are so strongly tied to property.

Private companies are fully permitted and protected, and the privatization process began in the late 1980s, when Croatia was part of Yugoslavia. Previously, all companies were within the system of social ownership. Privatization continued after 1992 when the Croatian Privatization Fund was founded, which managed the conversion of social enterprises into the state and private companies through the sale and transfer of shares and rights in the former socialist enterprises. Various methods of privatization were experimented, including privatization through worker's and manager's shareholding, through coupon privatization and selling through public offerings.

Currently, the privatization of state-owned shares in companies (whether majority or minority state owned) is conducted through public tendering and auction sales on the Zagreb stock exchange. The share of state-owned or local government-owned companies in the economy is relatively large. Of the top 50 companies, as measured by value added in 2017, 16 were majority or minority state owned. The last three governments' plans to privatize state-owned companies or sell state shares in private companies have largely failed. Goran Marić, minister of state property, suggested at the end of 2017 that the government should reduce state ownership and direct state funds to strategic economic sectors (e.g., energy, transport and water supply) instead of engaging in almost all sectors of the national economy. Marić concluded that Croatia has the highest share of state-owned companies of any European country, with over 1,100 companies involved in all sectors of the economy, whose contribution to budget revenues is small due to poor financial performance. However, by the end of January 2019, the Croatian government had still not proposed any concrete future steps for the privatization of these companies.

Private enterprise

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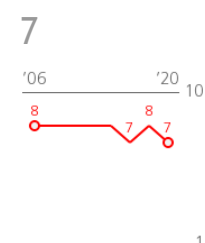
10 | Welfare Regime

Croatia's social safety nets cover only part of the risks that citizens face. Croatia ranks among the EU member states with the lowest level of welfare coverage, because a large portion of the overall social protection expenditure is earmarked for other purposes. However, the percentage of the population receiving welfare benefits has decreased substantially over the past five years. Compared to 112,000 welfare beneficiaries in 2013, when Croatia was in recession, there were 87,000 beneficiaries in late 2017 (2% of the population). Most social protection system funds are allocated for pensions and old age-related risks (approximately 35% of overall social protection expenditure), which is still below the EU average (40%). Approximately one-third of the overall social protection expenditure goes to health care (somewhat above the EU average). However, disability welfare expenditure is almost twice the EU average at more than 12% of the overall social protection expenditure. The benefits allocated for families and children in Croatia account for only 7% of the overall expenditure (below the EU average). Unemployment benefits account for a mere 2.5% of the overall social protection expenditure (EU average above 5%). Only 20% of those registered with the Employment Service receive cash benefits. When the more-than-proportional amounts spent on pensions and other benefits for war veterans are taken into account, the condition of the social protection system seems even less favorable.

Among those facing the highest risk of poverty are single-person households (particularly women), single-parent families and families with three or more children, as well as the unemployed, unskilled workers and workers employed in jobs that can be outsourced. The at-risk-of-poverty rate in 2017 was 20%, while the rate of people at risk of poverty or social exclusion was 26.4%. Both indicators are somewhat above the EU average. Also exceeding the EU average is the percentage of people severely materially deprived in Croatia, 10.3% in 2017 (although seven EU member states rank even worse). However, the percentage of severely materially deprived people has decreased substantially in the past years (in 2012, it was as much as 15.9%).

Welfare benefits and various types of assistance have reduced the poverty rate by approximately 25% (compared to the EU average of above 32%). Croatia's Gini coefficient was modest at 29.9% in 2017 – lower than the EU average of 30.7%, but higher than in neighboring Slovenia. Similarly, the ratio between the highest and lowest earning quintiles is lower in Croatia (4.8) than the EU average (5.2).

Social safety nets



Laws for equal opportunity are well developed due to EU integration, but problems persist, especially in terms of ethnic segregation, with Roma (who suffer from very low levels of school attendance) and Serb communities particularly affected. On the other hand, female participation in the labor force is fairly high at 46.3% (2018), and school enrollment rates for girls and boys are equal, and higher for women in tertiary education.

However, enrollment rates in tertiary education vary greatly by socioeconomic background, with Croatian students from lower socioeconomic groups underrepresented. This is why many higher education policy experts believe that the Croatian higher education system is not inclusive. Research has shown that children from higher socioeconomic backgrounds are six times more likely to access higher education than children from poorer backgrounds.

Unequal access to education is perhaps even more noticeable among younger populations. Research has shown that 22% of Croatian children from poorer backgrounds are enrolled in kindergarten, which is by far the lowest percentage in a survey of EU member states and Iceland. Of children from wealthy families, 70% attend kindergartens.

Significant differences have also been observed in regional social-assistance-dependency rates. In the areas along the border with Bosnia and Herzegovina that were strongly affected by the war in the 1990s, the share of social assistance beneficiaries often ranges between 8% and 15% of the population. The percentages are similar in Slavonia (between 6% and 8% even in cities). On the other hand, the share of social assistance beneficiaries in the wealthier municipalities in western and northwestern Croatia, and in the major tourist destinations on the Adriatic coast generally does not exceed 1%, or often even 0.5%.

Equal opportunity

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11 | Economic Performance

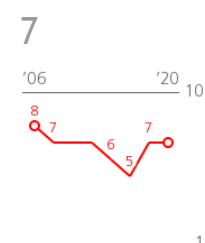
From the second half of 2015, following six years of recession, the Croatian economy grew for 18 successive quarters. The per capita GDP growth rate accelerated to 4% in 2016 and 2017. Inflation has slightly increased (1.1% in 2017 and 1.5% in 2018), but remains low and stable. In the review period, external debt reduced significantly, from €41.6 billion in 2016 to €38.7 billion in September 2018. The current account balance surplus was equivalent to 4.0% and 2.9% of the GDP in 2017 and 2018, respectively. After a significant drop in FDI inflows in 2015 to 2016, inflows slightly increased in the review period, but the amounts remain below those recorded before the 2009 economic crisis.

Strong consumer spending and investments have had a positive impact on economic growth in period after 2015. However, because of the decrease in industrial production that began in 2018 and the failure to increase exports, GDP growth was estimated to have slowed down in the fourth quarter of 2018. The real GDP growth rate is gradually approaching the potential growth rate, which ranks the lowest among EU member states in Central and Southeastern Europe. Of the factors affecting potential GDP, the low utilization of the labor force remains the most questionable. The share of the working-age population has been dropping continuously since the outbreak of the economic crisis in 2009. Ever since Croatia's accession to the European Union, emigration has significantly increased. However, total factor productivity has also been low, substantially limiting possibilities for strong economic growth.

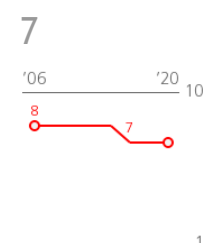
12 | Sustainability

Environmental policy in Croatia since 2013 has been strongly shaped by Croatia's accession to the European Union. The Croatian government is obliged to spend significant sums of money on coping with environmental requirements in waste management, water management and air protection. The implementation of required policies in the environmental sector has, however, progressed slowly and sometimes is envisaged by the EU infringement procedures. In early 2017, the HDZ-Most coalition government adopted a new medium-term waste management plan, which partially fulfilled the European Commission's concerns. Nevertheless, several major challenges in Croatia's environmental protection policy still remain, particularly in water management and waste management. In the water management sector, substantial investment in the public water supply and drainage system, and wastewater treatment system is essential, as there is a high percentage of water loss (48%) in the system. Progress in waste management has also been inadequate. Of 12 planned regional waste management centers, only two have been completed – both in the western part of the country, in Istria and the region around the city of Rijeka.

Output strength



Environmental policy



Another problem is the fact that these planned waste management centers will be focused primarily on mixed municipal waste and not on various environmental policy measures that would promote the development of a circular economy (e.g., selecting, separating and reusing waste).

Access to education is open and broad, and the share of early school and vocational training leavers is far below the EU average. However, upper-secondary education is unbalanced. Approximately one-quarter of upper-secondary aged pupils attend high schools, while the rest attend vocational education institutions. Vocational education is, however, very weak and there is a high degree of discrepancy between what is taught in vocational education institutions and demanded by employers. Therefore, vocational education does not represent a reliable path into employment. The quality of tertiary education varies significantly across institutions and even between departments within universities.

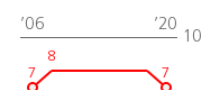
The education reform launched by the Milanović government in 2014 has suffered from a lack of continuity. An expert team provided a comprehensive proposal for a new primary and secondary school curriculum, but the implementation of the reform was delayed until September 2018, when the new minister of science and education finally piloted an experimental curriculum. Expectations for the pilot are great, with the experimental curriculum intended to strengthen students' problem solving and critical thinking skills by moving away from merely teaching facts. The government's intention is to scale the experimental curriculum into a full-scale educational reform, with the goal of reversing the negative trend in educational outcomes. The reform is also expected to improve vocational education students' prospects of finding employment after completing their education.

The next step in higher education reform will involve reorienting the sector toward STEM disciplines. The policy is based on the belief that students should be selectively encouraged to enroll in colleges with STEM disciplines instead of humanities and social sciences, because it will ensure better coordination between the labor market demand and higher-education programs.

Croatia does not have a coherent and integrated R&D policy framework, and investments remain far below 1.5% of GDP, the target suggested by the European Commission. In 2017 and 2018, spending on R&D was around 0.8% of GDP, compared to more than 2% in the EU-28. This was mainly due to the very low level of expenditure on R&D by the business sector, which spent only 0.44% of GDP on R&D.

Education policy /
R&D

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Governance

I. Level of Difficulty

Structural constraints in Croatia primarily have to do with labor supply and uneven levels of regional development. The GDP of the City of Zagreb exceeds the EU average by 6% and the Croatian average by 75%. Only three areas exceed the Croatian average: Istrian county, the Greater Rijeka area in the Primorje-Gorski Kotar county and Dubrovnik-Neretva county. Five counties, mostly in Slavonia, are more than 40% below Croatian average.

Another important structural constraint is labor supply. In recent years, Croatia has experienced a substantial decrease in its working-age population. Since there has not been any relevant decrease in the share of the economically non-active population, labor supply has become a constraining factor on economic development. The labor supply has been maintained to some extent by a decrease in the share of the unemployed in the non-active population. However, it seems that this source of labor supply has been exhausted. Immigration policy remains the only solution to this problem; however, it is still not being implemented systematically in Croatia.

The roots of Croatian civil society date back to the socialist period when the country was part of Yugoslavia, a relatively liberal state among the communist countries. In mid-1980s, the first independent groups advocating new environmental policy, gender issues and human rights appeared. The war that broke out in Croatia in 1991 significantly inhibited civil society development, instead promoting ethnonationalist homogenization of society and strong identification with the national state. After the war, in the second half of 1990s, civil society developed rapidly as a series of NGOs were established, trade unions strengthened and other forms of associations created.

Croatia performs well on the criterion of organization and structure of civil society, helped by the establishment of the Government Office for Cooperation with NGOs. While the policy-making impact of civil society in Croatia remains weak compared to developed European democracies, there are indications that things are starting to improve. Over the last couple of years, several civil society organizations have developed their own capacities to set agendas and to propose policy in particular fields. However, public participation in civil society initiatives is still low, and there has been a failure to establish sustainable cooperation between civil society organizations, and government and business associations. Among civil society organizations, there is also a lack of transparency, little networking between

Structural constraints

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Civil society traditions

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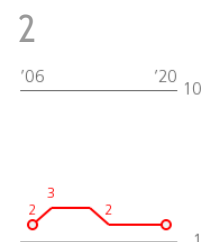


organizations, and a heavy dependence on foreign and domestic public funding. Especially the politically influential war veteran's associations receive significant support from the state.

Regardless of their structural weaknesses, various NGOs strive to act decisively in protecting human rights and freedoms. In September 2018, several NGOs strongly criticized the continued politicization of Croatian Radiotelevision (Hrvatska radiotelevizija, HRT) and the political pressure exerted on its journalists. This criticism was provoked by the dismissal of Hrvoje Zovko, a HRT journalist and program editor who resigned on account of censorship and pressure to change his editorial policy. In reports covering 2017 and 2018, a number of NGOs also argue that human rights protections, while formally in place in Croatia, are inadequate. In their opinion, one of the key reasons for this is the fact that the protection of human rights is still not among the top priorities of Croatian governments. According to the NGOs, the fact that the new National Program of Protection and Promotion of Human Rights has still not been adopted, although the old program expired in late 2016, is evidence of this.

There are no strong social, ethnic or religious conflicts of any relevant intensity in Croatia today. The social conflicts are negligible: the socioeconomic differences (which are of moderate intensity) arise primarily from regional differences. Stricken by economic hardships, devastated industry and poor status of agriculture, the eastern region (Slavonia) has been facing an extremely high rate of labor drain to other European countries, a phenomenon suppressing potential conflicts of social nature. Croatia is ethnically very homogeneous, with Croats accounting for 90.4% of the population. Serbs rank second (4.4%), while no other ethnic group exceeds 1%. The country's national structure underwent a radical change after the war that had followed the disintegration of Yugoslavia (1991-1995). Before that, Croats accounted for 78.1%, Serbs 12.2%, and Yugoslavs 2.2%. After the bitter conflict between Croats and Serbs in the early 1990s – when Serbs gained control over one-third of Croatia's territory with the help of the Yugoslav army and Serbia for several years, not just of the predominantly Serb-populated areas – the intensity of the conflict gradually subsided after the mid-1990s. The peaceful reintegration of the country's easternmost parts (the Danube Region) into the constitutional order marked the beginning of a new perspective for Croat-Serb relations. After that, the two communities coexisted peacefully in this part of Croatia, but only as separate social systems (including separate school systems and despite some issues with minority rights).

Conflict intensity



II. Governance Performance

14 | Steering Capability

Croatian public administration is strongly centralized, with central government playing a much greater role than local government in public service provision. By European standards, the system is relatively ineffective due to shortcomings in policy formulation, and the fragmented and ineffective implementation of policies. Policy formulation is characterized by poor strategic planning, weak policy coordination, a lack of evidence-based policy-making and limited participation of non-government stakeholders in policy-making. As a result, the level of prioritization of fundamental policy goals is low. Although some progress has been made due to the process of Europeanization, the quality and inclusiveness of strategic planning tools in policy-making is of very poor quality. Hence, central, regional and local governments face problems in determining policy priorities. Research on strategic documents prepared by central and subnational governments since the 1990s suggests that these documents are often incomplete. The most reliable and effective organization within the Croatian public administration is the tax administration, which is vertically organized and offers a high-quality digital service.

Public policy implementation in Croatia is characterized by the partial success of the central government in achieving its policy objectives. The executive's effectiveness in monitoring line ministries is low, while vertical coordination between central government and local self-governments is poor. Inefficient implementation remains one of the biggest challenges faced by the Croatian government.

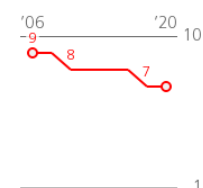
Ineffective implementation is reflected in the fact that the Croatian government usually only manages to implement (fully or to a large extent) a fifth of European Commission recommendations each year. The same number of recommendations are not implemented at all, while very limited progress is made on 30% of recommendations. A lack of strong policy monitoring capacities is evident across a number of sectors.

During the review period, Croatia continued to face substantial challenges in implementing economic reforms and fostering economic competitiveness. According to the Doing Business data, Croatia failed to improve the competitiveness of its national economy. One of the reasons for this is that in 2017 and 2018 Croatia only implemented two economic reforms: a relatively successful tax reform and a partial pension reform. Along with the stability of public finances and the gradual reduction of public debt, these were the only advances in economic reform during the review period.

Question
Score

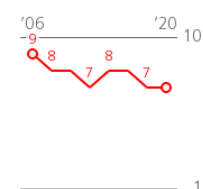
Prioritization

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Implementation

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Greater success has been achieved in education reform, strongly supported by Minister of Science and Education Blaženka Divjak. In September 2018, a pilot of a new curriculum, School for Life, was launched in 74 primary and secondary schools, with the plan to broaden the reform to all primary and secondary schools in September 2019.

The national government has still not articulated a comprehensive policy to cope with the biggest challenge facing Croatia today: the extremely high rate of emigration.

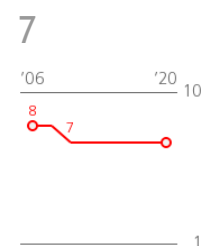
The government has not demonstrated a fully adequate level of innovation and flexibility in policy learning. In regular EU reports on the coordination of economic policies within the framework of the European semester, Croatia has been regularly criticized for the slow implementation of crucial public policy reforms and for the failure to fulfill requirements for policy innovation. The European Commission regularly criticized the involvement of small horizontal policy stakeholders in the formulation of public policies, and the low capacity of policy monitoring and evaluation of effective public policies to be implemented. The European Commission also regularly pointed to the under-involvement of experts in the development of key policies.

While the Public Administration Strategy was adopted by the parliament in 2015, no systematic public administration reform subsequently appeared, and reform was restricted to merging or reducing the number of agencies. A public administration reform plan proposed at the beginning of 2016 included three important directions: the digitalization of public administration; the systematic analysis of human resources (including competence analysis, analysis of public administration tasks and a review of the process of awarding salaries), with the aim that all equivalent jobs receive the same pay; and the proposal to rationalize the organization of central government, local and regional governments (including ministries, agencies).

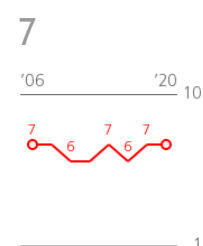
15 | Resource Efficiency

When the Plenković government proposed the 2017 and 2018 state budgets, the total projected deficit was lower than in preceding years. The state budget deficit for 2017 was 1.8% of GDP, while the projected deficit for 2018 is 1.9%. Due to the surplus realized in extra-budgetary funds, the total consolidated government budget surplus was 0.7%. During the review period, a reliable fiscal framework was finally established, which contributed to a relatively balanced budget and prevented any further increases in the public debt. The result of the government's fiscal policy achievements combined with continuous economic growth was a reduction in the public debt ratio, which by the end of 2018 was 75% of GDP – a substantial reduction from its peak of 86.5% in 2015.

Policy learning



Efficient use of assets



The National Audit Office's control over public spending has strengthened considerably. After the law on internal control systems in the public sector was enacted in 2015, which requires all budget implementers to publish a statement on fiscal responsibility, further steps in achieving fiscal responsibility were developed. In 2018, the parliament passed a new fiscal responsibility law and prepared the new State Audit Office Act for adoption in 2019.

In 2018, however, there was an increased risk of the state having to deliver on guarantees to the Pula and Rijeka shipyards, which faced severe financial difficulties and had become a further burden on the state budget.

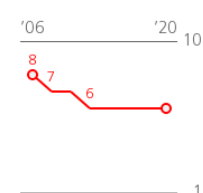
For a while now, experts on the Croatian government have been warning that one of the major problems of governance lies in the lack of horizontal coordination between ministries, and vertical coordination between ministries and the government. Attempts to avoid various overlaps and problems in establishing integrated policies in particular sectors can best be seen in the Ministry of Science and Economy's failure to introduce an integrated innovation policy. This case clearly reflects poor inter-organizational communication, and an inability to resolve disputes between ministries in the formulation and implementation of common policies. It also reflects the lack of arbitration mechanisms for such cases, which would ensure the implementation of a single, integrated government policy. Two key problems in policy coordination are the government's inability to arbitrate interministerial disputes and failure to establish a clear policy framework for ministries to abide by. As a result, government priorities are often rather unclear.

Since the adoption of the first multi-annual anti-corruption plan in 2006, Croatia has gradually developed an elaborate institutional framework, which should reduce the level of corruption in the country. The requirements for EU membership forced the government to reform the state apparatus in order to tackle corruption. The plan was based on improving the transparency and efficiency of state institutions. Since 2008, an anti-corruption strategy proposed by the government and adopted by the parliament established the National Implementation Monitoring Council, headed by a representative of the opposition, and a commission for monitoring the implementation of anti-corruption measures, chaired by the minister of justice. The Ministry of Justice is also tasked with drafting action plans in line with the government's anti-corruption strategies, which defining the preparation and implementation of anti-corruption policy measures.

Based on this institutional framework and EU pressure on the government to act decisively against corruption, corruption has gradually begun to decrease. In many areas, however, strict enforcement has been limited to the formal adoption rather than the effective implementation of anti-corruption measures. Analysis by GRECO has shown that corruption is still widespread in the judiciary, while other reports suggest that corruption continues to exist in the funding of political parties and election campaigns, public procurement, employment in public companies and public

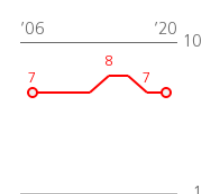
Policy coordination

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Anti-corruption policy

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administration, among other areas. This has been backed up by the fact that few high-ranking officials have been found guilty of corruption, despite cases being brought against former prime minister Sanader, Zagreb mayor Bandić, and several former ministers and other officials. Nevertheless, progress has been made in some areas, including tighter monitoring of central government and subnational government budget spending, and greater control over political party financing. Furthermore, the Conflict of Interest Commission has been more effective since Dalija Orešković became chair of the commission in 2013.

The efficiency of anti-corruption policy has decreased and the perception of corruption increased as a result of the Agrokor scandal. Meanwhile, the number of party defections is increasing, with many defections believed to be motivated by financial or other benefit and suspected of corruption in public procurement. For these reasons, the very high level of corruption remains one of the most significant obstacles to further socioeconomic development in Croatia.

16 | Consensus-Building

In Croatia, there is a consensus on the importance of democratic institutions and threat posed by hate speech to democracy. But problems arise when defining exactly what constitutes hate speech and strong differences appear, which reflect the key historical cleavages that marked Croatia in the 20th century. The fundamental problem in these disputes relates to different understandings of the function of the state. Achieving consensus on key development objectives enhances the state's capacity to formulate and implement public policy. However, this type of consensus in Croatia is a major challenge. So far, political consensus has only successfully been achieved in determining whether Croatia should join the European Union.

Ethnicity is central to understandings of democracy in Croatia. Hate speech and minority rights are not seen as priorities in Croatia. Nevertheless, acceptance of the need to adhere to EU standards across the political spectrum means that hate speech and minority rights in Croatia are usually in line with EU standards, although there is an underlying risk of backsliding.

In Croatian society, there is a relatively clear commitment of key stakeholders (e.g., politicians in power, leading political parties, business associations, trade unions and NGOs) to the development of Croatia as a democratic country with a social market economy. Problems arise when determining long-term policy goals and the principal policies that will lead to the accomplishment of these goals. A good example is the concept of the social market economy. This is in some ways a general goal that is followed by both major political parties (the HDZ and the SDP). However, the HDZ and SDP have somewhat different visions for reform of the labor market, education system and pension system, which will be necessary for the development of a social market economy. However, even minor differences prevent political parties from

Consensus on goals

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reaching agreement on the basic elements of these policies. At the beginning of each government term, these elements are called into question and policies are redeveloped from the scratch. This problem is evident in almost all policy areas, including demographic renewal, sustainable environmental management, reform of the local government, development of agriculture and rural areas.

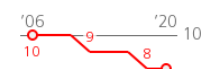
Anti-democratic political actors in Croatia are mainly related to right-wing parties and NGOs that use extremely conservative, nationalist rhetoric and generally perceive opponents of Croatian nationalism in all institutions that should be politically eliminated whenever possible. Such parties have been given a certain impetus since the elections in November 2015, when the HDZ gathered a wide range of parties, which included some parties that strongly advocated nationalist rhetoric. In the September 2016 parliamentary elections, these right-wing parties failed to enter the Croatian parliament, but the HDZ included several politicians among its parliamentary deputies whose rhetoric is strongly linked to all forms of ethnic exclusiveness. While the moderate conservatives within the HDZ succeeded in appointing Andrej Plenković as prime minister and HDZ president, and marginalizing the radicals, the moderate center-right politicians nevertheless failed to clearly distance themselves from right-wing extremists and their ideology.

In addition, there is a whole range of NGOs that strongly advocate radical conservative ideas, oppose gender equality and advocate a ban on abortion rights. Among the anti-democratic groups there are a couple of extra-parliamentary political parties, which have little political influence, but occasionally organize political rallies whose origins could be traced to the tenets of the Independent State of Croatia (a puppet fascist state from 1941 to 1945). In the army or within the powerful economic groups, there are no significant anti-democratic veto-actors.

Key political actors agree that a democratic political system and a market economy form the basic institutional framework for further development in Croatia. In the political arena, there are actors who promote a strong populist attitude that question several standard mechanisms of the market economy, but such views do not yet represent a comprehensive platform that would challenge the institutional framework of a market economy. Political groups that openly question the basic mechanisms of a democratic political order are quite marginal. The basic cleavage that exists in Croatian society primarily concerns the extent to which the idea of the Croatian nation and the institutional role of the Catholic Church should be the primary source of political action, and the development of state and society. Those cleavage-based conflict that do exist are rooted in the country's fascist period (1941-1945) or period of one-party socialist rule (1945-1990). Citizens who believe that the idea of the nation and the Catholic Church should have an important place in Croatian politics strongly support the right-center political parties, while citizens who feel that the role of these factors should not be overstated support the left-centrist parties. Class polarization is in fact almost completely irrelevant, but where it does exist, it has a

Anti-democratic actors

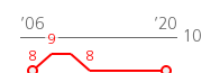
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Cleavage / conflict management

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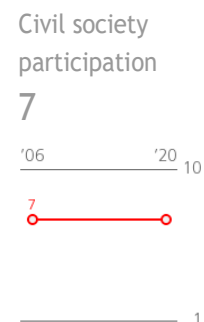
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regional dimension. In the east, south, and in areas along the border with Bosnia and Herzegovina, there is a significantly greater attachment to the idea of the Croatian nation and the role of the Catholic Church, than in the more developed western and northwestern parts of the country.

Civil society in Croatia shares many shortcomings with other post-communist countries, especially Western Balkan countries. Key weaknesses include the low level of public participation; the lack of meaningful and sustainable cooperation between civil society organizations, and government and business associations; the general lack of transparency; the limited networking between civil society organizations; and the reliance of civil society organizations on foreign and domestic public funding. Domestic government funding has given conservative civil society organizations more influence than others, especially if organizations connected to traditional nation- and state-building projects or to the Catholic Church.

However, the involvement of civil society in public policy-making processes has improved due to the systematic monitoring of implementation of the Code of Practice on Consultations with the Interested Public in Procedures of Adopting Laws, Other Regulations and Acts. The code strongly supports the involvement of civil society actors in all phases of policy-making, particularly in policy formulation and implementation. The European Commission also strongly supports the more active involvement of civil society in the policy-making process. When Croatia and many other post-communist countries, particularly from the southeastern Europe, are compared with the more mature democracies of western and northern Europe, it is evident citizens in post-communist countries rarely participate in civil society activities because they lack trust in others, and prefer to engage with family members and close friends. That is probably the crucial reason why post-communist countries are predominantly based on informal relations, where informal practice represents a kind of social norm, strongly shaping people's behavior.

However, in recent years, a new trend in conservative NGOs has been noticeable. After successfully organizing a referendum on the constitutional definition of marriage in late 2013, conservative NGOs launched two referendum initiatives in 2018. The first initiative advocated the rejection of the Declaration of Istanbul, which was strongly supported by the Catholic Church. The second initiative demanded amendments to electoral legislation, which would deny ethnic minority members of parliament the right to vote on a no-confidence motion or on the adoption of the state budget. In mid-June 2018, the two referendum initiatives, "People's Choice" and "Truth about Declaration of Istanbul," were submitted to the parliament having apparently secured more than 400,000 and 340,000 signatures, respectively. However, at a government session in mid-October 2018, Minister of Public Administration Lovro Kušević reported that more than 40,000 signatures to each initiative were invalid and, as a result, both initiatives had failed to collect the required number of signatures (10% of the overall number of registered voters) to



force a referendum. The Croatian parliament will consider the issue in February 2019. It is expected that the parliament will confirm Kušćević's statement, because the ruling HDZ and HNS, and most center-left members of parliament oppose the initiative of the conservative NGOs.

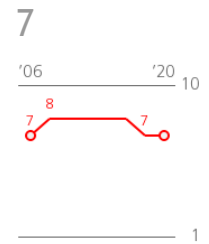
Relatively strong divisions still persist related to the events of 1941 and 1945, during the existence of the Independent State of Croatia (NDH). Dealing with the past in Croatia remains an extremely fractious and painful process, which results in completely opposing interpretations of the tragic events during and immediately after World War II. Croatia's divisive history has recently become more important factor for political mobilization and framing. While right-wing extremists within the HDZ do not deny their admiration for the fascist NDH regime, the social democrats are framed as neglecting the crimes committed by the communist regime. In 2017, the Council for Dealing with the Consequences of the Rule of Non-Democratic Regimes was formed to deal with the past and address the complex conflicts regarding these issues that persist. The task of the council is not to determine what happened in the past (i.e., the truth), because it is a matter of serious historiographical research. Instead, the task of the council was to achieve a minimum consensus on the past and enable Croatian society to cope with the past. At the beginning of 2018, the council, consisting of 17 members (historians and other intellectuals), prepared documents, among other things, recommending how to treat insignia of totalitarian regimes. The document clearly condemns totalitarian regimes, including the 1941 to 1945 Nazi-style Ustasha regime and the Chetnik movement. The document concludes that the "For the Homeland Ready" salute, which was used during the period of the collaborationist Independent State of Croatia (1941 – 1945), has an anti-constitutional character. Consequently, the salute should only be used for commemorative purposes for slain members of the Croatian Defense Forces, the armed wing of the Croatian Party of Rights during the 1991 to 1995 war.

Contradictory memories related to the 1991 to 1995 conflict and the Croatian military operation to liberate the so-called Serbian Krajina from Serbian insurgents in 1995 prevents reconciliation between Croatia and Serbia, as well as ethnic Croats and Serbs. Whereas Serbia commemorates the conflict as the expulsion of Croatia's ethnic Serb community, Croatia celebrates it as a great military victory. The Serb minority in Croatia is treated as a security threat.

The Croatian state continues to hold trials in absentia for Serbs. Croat perpetrators are prosecuted, although participation in the conflict is seen as a mitigating circumstance and trials are often abandoned.

Croatian state involvement in the Bosnian conflict continues to be denied, despite rulings at the International Criminal Tribunal for the former Yugoslavia showing that the Croatian state supported Croat forces in Bosnia-Herzegovina.

Reconciliation

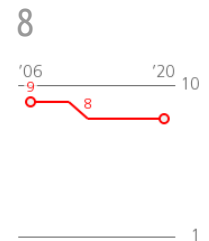


17 | International Cooperation

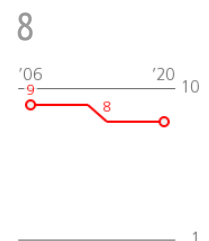
Croatia has made some progress in the planning of political and economic development, which is also the result of Europeanization. EU membership for Croatia, as one of the least developed member states, is of great importance and the Croatian authorities are trying, by aligning their actions with the European Commission, to improve the country's development. The European Commission has repeatedly stated that the alignment of policies should be faster, as Corina Cretu, European Commissioner for Regional Policy, stated when visiting Croatia at the beginning of 2017. Cretu said that Croatia must accelerate the implementation of EU funded programs. Since 2013, when the Milanović government refused to apply the European Arrest Warrant for Perković (an influential communist-era security official suspected of organizing the murder of an exiled dissident in Germany), Croatian authorities have not had any major disputes with the European Commission. However, Croatia has still not achieved a satisfactory level of effectiveness in the use of EU development mechanisms (especially in cohesion policy, and agriculture and rural development) to promote domestic development. The European Commission has regularly warned Croatia about the country's shortcoming within the procedures of the European Semester.

The government mostly acts a credible and reliable partner in its relations with the international community. This applies equally to relationships with multilateral and intergovernmental organizations, as well as in relations with the governments of other countries and some international NGOs. Cooperation with the International Criminal Tribunal for the former Yugoslavia was a precondition for the start of negotiations on Croatian membership in the European Union. The Perković case (the controversial extradition of a communist-era secret-service agent charged with killing a Croat emigrant) was resolved in early 2014 with his extradition to Germany. The Orešković government declared its readiness to host a share of refugees as agreed by EU interior ministers in 2015. The Plenković government, which took office in October 2016, has several times stated that Croatia is ready to host refugees. Cooperation with the international community, multilateral organizations and international organizations in the field of environmental protection is very productive. The problems of credibility in relations with the international community largely affect foreign investments. The dispute bureaucracy and complicated legal system significantly undermines foreign investor confidence, which could significantly contribute to the growth potential of the Croatian economy.

Effective use of support



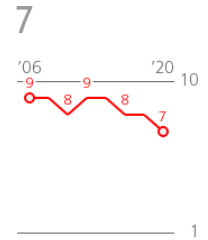
Credibility



Political cooperation between Croatia and other countries in the region is not at the level as economic cooperation between Croatia and other countries of the former Yugoslavia. Political cooperation with Serbia is particularly problematic, especially after the International Criminal Tribunal for the former Yugoslavia had temporarily released the Serbian ultra-nationalist Vojislav Šešelj. Relations were further exacerbated by the refugee crisis in 2015 and exchanges of hostile public statements between the Croatian and Serbian prime ministers. In 2016, Croatia blocked the opening of two EU accession negotiation chapters with Serbia for several months in order to force Serbia to repeal a law that had authorized its courts to prosecute war crimes committed throughout the former Yugoslavia. Croatian war veterans' organizations feared a wave of European arrest warrants after Serbia's accession to the European Union.

In December 2016, Croatian President Kolinda Grabar-Kitarović said in Dubrovnik that authorities in the Balkan region should face the fact that several thousand former Islamic State (IS) group fighters will return to Bosnia and Herzegovina. Bosniak war victims have accused Croatia's president of damaging Bosnia and Herzegovina with inappropriate claims that the country is turning into a hub for Islamic terrorists. In September 2017, several Bosniak war victims' associations signed an open letter to Kolinda Grabar-Kitarović opposing her suggestion that Bosnia and Herzegovina is a threat to regional stability because of Islamic radicalism. The victims' associations, headed by the Mothers of Srebrenica, accused Grabar-Kitarović of "causing damage to Bosnia and Herzegovina." Tensions with Bosnia and Herzegovina escalated in 2018 when both Croatia's prime minister and president openly criticized the outcome of the election for the Croat member of Bosnia and Herzegovina's collective presidency.

Regional cooperation



Strategic Outlook

Croatia has been an EU member state since 2013. However, its economy still lags behind the economies of comparable countries in Central and Southeastern Europe. The low economic growth rate is the fundamental economic challenge facing Croatia today. The country's dominant development approach – which is exclusively focused on increasing earnings from tourism and real estate sales and lacks an appropriate industrial development policy – has proven to be a failure.

A series of reforms is necessary to accelerate productivity growth and the adoption of innovations, increase the labor market participation of the working-age population, and significantly raise competitiveness and improve the business climate in the country. These measures would substantially increase Croatia's potential GDP, which is currently 1.9%. The main problem concerns the share of labor in the potential product due to the extreme reduction in the working-age population and emigration of skilled workers to other European countries, with most emigrating to Germany. Total factor productivity linked with efficient economic processes should also be substantially improved.

Basic fiscal sustainability has been attained. However, fiscal policy remains the government's key challenge, as public debt remains very high. The problem is related to the drivers of GDP growth. Economic growth in Croatia is based largely on increasing household consumption, which in turn has been based on a reduction in income tax. This will not be sufficient for convergence with EU levels. Solving this problem could help increase the participation of the working-age population in the labor market, particularly people above the age of 50, because no measures have been developed for increasing the activity of people aged over 50. In addition, the number of working-age people has been continually declining since Croatia joined the European Union.

Croatian GDP has been growing slower than in comparable countries due to a slower growth in exports in Croatia and the lower share of technologically complex products exported by Croatia. Increasing the export of technologically complex products, with average salaries significantly higher in these industries, will help retain skilled workers. A connected challenge involves increasing the level of investment and changing the structure of investments. Private sector actors point out that their investment capacities are reduced due to excessive tax levies and quasi-taxes, and the inflated wage bill necessary to retain skilled labor. Changing the structure of investments is equally important, as most investments are linked to real estate due to the high share of tourism in the country's GDP. Public sector investments are very low and usually depend on EU funds, indicating a lack of reform in public enterprise management.

The fourth challenge is related to the necessity for public sector reforms, particularly in health care and education, which will directly impact the quality of human capital. The health care system is facing serious financial difficulties and functional problems, which affect patient waiting times, treatment outcomes and health care availability. For this reason, introducing more effective health care policies will be one of the key challenges in the years to come. Education reforms have been

launched, but they need to be more comprehensive and carried out faster. The final challenge will be reforming the judiciary and public administration. Judicial and public administration reform has not taken place, which is a key constraint on achieving more dynamic economic growth.

However, an essential prerequisite for the development of all these policies will be the further development of democracy in Croatia. Jeopardizing further democratization is the growth in populist tendencies, which often acquire a radical-conservative form. Therefore, Croatia's current political leaders have a historic responsibility to promote the fundamental values of democracy – including the protection of ethnic and gender minority rights, and the right to abortion – by building on existing legal frameworks. In order to achieve more dynamic economic growth, which would lead to convergence with other European countries, a crucial precondition is institutional quality and stability. Achieving this will require strengthening various forms of policy capacity at all levels of governance, while ensuring a more equitable distribution of support for civil society organizations.