

# BTI 2014 | Croatia Country Report

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This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2014. It covers the period from 31 January 2011 to 31 January 2013. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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**Key Indicators**

Population	M	4.3	HDI	0.805	GDP p.c.	\$	20532.0
Pop. growth <sup>1</sup>	% p.a.	-0.3	HDI rank of 187	47	Gini Index		33.7
Life expectancy	years	76.9	UN Education Index	0.784	Poverty <sup>3</sup>	%	0.1
Urban population	%	58.1	Gender inequality <sup>2</sup>	0.179	Aid per capita	\$	0.1

Sources: The World Bank, World Development Indicators 2013 | UNDP, Human Development Report 2013. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$2 a day.

## Executive Summary

Croatia experienced a number of political and economic developments during the review period. Criminal proceedings against former high-ranking politicians proceeded apace. Negotiations over Croatia's accession to the European Union were completed in mid-2011. In December 2011, amid parliamentary elections the Croatian Democratic Union (HDZ) lost power and the Social Democratic Party of Croatia (SDP) formed a new coalition government. And finally, the effects of the economic crisis, begun at the end of 2008, have yet to abate.

In November 2012 a court in Zagreb convicted former Prime Minister Ivo Sanader on corruption charges and sentenced him to 10 years in jail. He was found guilty of accepting bribes for brokering a loan between the government and an Austrian bank in the mid-1990s, and for providing Mol, a Hungarian oil company, control over Croatian energy company Ina in 2008. While other corruption cases against other politicians and businessmen continue, Sanader's case is unprecedented in the history of modern Croatia as he is one of the highest-ranking state officials to be indicted. The Sanader case, among the many corruption cases being heard, not only shows that a serious effort to fight corruption is finally underway but also outlines the extent to which corruption has spread through Croatian society.

Changes in the country's anti-corruption policy were one of the preconditions that enabled Croatia's closure of negotiations with the European Union. Croatia signed the accession treaty with the European Union and its member states on 9 December 2011. Croatia was scheduled to join the European Union on 1 July 2013; but at the same time, Croatia was placed under a monitoring program to last until the accession date. On 22 January 2012, nearly two-thirds of voters approved Croatia's accession in a referendum, yet the turnout was only 43.5%.

The economic crisis and exposure of corruption scandals involving the ruling elite were the main reasons why the HDZ lost the parliamentary elections on 4 December 2011. A four-party coalition led by the SDP achieved a majority of 53% in parliament, enabling the party to form a government

led by Prime Minister Zoran Milanovic. The new government continued a policy of building cooperation with neighboring countries, yet after the controversial right-wing candidate Tomislav Nikolic was elected president in Serbia, relations between Croatia and Serbia started to cool. The focus of the new Croatian government was on domestic economic and social policies, with the promise to pull the country out of the crisis, but by the end of 2012 Croatia's GDP continued to fall. The government introduced a tax reform and began the restructuring of large state-owned companies, but projects that were supposed to boost the economy, such as investments, fell short. Moreover, the government failed to implement structural reforms to reduce public spending, and at the end of 2012, this failure resulted in a reduction of Croatia's debt rating. Although Croatian economic analysts often forecast lower economic growth numbers than those anticipated by the government, it was precisely because of the country's expected entry into the European Union in 2013 that experts predicted higher GDP growth in coming years.

## History and Characteristics of Transformation

Croatia's transition to democracy and a market economy in the 1990s was accompanied and constrained by the wars following the breakup of the former Yugoslavia. Political liberalization and Slobodan Milosevic's nationalist mobilization campaign in Yugoslavia enabled the nationalist Croatian Democratic Union (HDZ) and its charismatic leader, Franjo Tudjman, to win the country's first democratic elections in May 1990. The new political leadership transformed Croatia into an ethnic nation-state by adopting a new constitution and by holding (and winning) a referendum on independence in May 1991. These actions evoked protests and militant resistance among ethnic Serb residents of Croatia (approximately 12% of the population in 1991). Croatia declared its independence in June 1991. Anticipating and responding to this act, ethnic Serb insurgents and units of the Yugoslav People's Army occupied territories in Northern Dalmatia, Lika, Kordun, Banija, Baranya and Slavonia that had been inhabited by ethnic Serb majorities. In 1995, Croatia's army re-established control over these territories, and most ethnic Serbs fled or were forced to leave.

After a decade of semi-authoritarian rule of by President Tudjman and the HDZ, an opposition coalition led by the Social Democratic Party (SDP) won the 2000 parliamentary elections. That was a boost to democratization in Croatia. These critical elections heralded a break with the previous hybrid regime and they forced HDZ to reform itself. During its period in office, the new government introduced institutional changes that aimed to strengthen the role of parliament and government in creating and implementing policies, to stem irregularities in the privatization process which were common in the previous decade and which destroyed part of the economy, and to increase the level of civil and political rights and freedoms in the country. Constitutional changes affected the abandonment of a semi-presidential system of government in favor of a parliamentary system. The presidency was thus deprived of the ability to control the government, and thereby each subsequent office holder who might attempt to replicate the autocratic style of President Tudjman has been stymied. The arrival of a new class of political elites changed the

behavior of politicians in general, and the government and the opposition in particular, because new criteria for behavior in politics were set. This brought about a shift in the political culture of citizens too, as it changed their attitude toward politics and strengthened their expectations of the political elite toward a stricter observance of the legal order.

Further steps toward democratization were difficult as the legacy of the 1990s wars weighted heavy on politics and society. Citizens continued to be split over Croatia's responsibility for crimes committed during the wars that were linked to the disintegration of the former Yugoslavia. Right-wing opposition parties, influential associations of Croatian war veterans and political actors within the SDP-led coalition government opposed the extradition of Croatian army generals indicted of war crimes by the International Criminal Tribunal for the Former Yugoslavia (ICTY). In 2002, the coalition government collapsed, and during the entire period the political right criticized cooperation with the ICTY.

Nevertheless, as the HDZ returned to power in 2003, the party did not signal its reluctance to cooperate and extradite indicted Croatian war criminals to ICTY. The best example of this was the arrest of fugitive General Ante Gotovina in 2005, which was conducted by the HDZ-led government.

Joining the European Union and the North Atlantic Treaty Organization (NATO) were important factors influencing Croatia's political transformation and democratization. Both organizations, especially the European Union, offered clearly defined criteria for Croatian membership. This is particularly true for judicial reforms, the fight against corruption and emphasis on foreign policy, which should contribute to the stabilization of southeastern Europe. Croatia joined NATO in 2009 and completed its negotiations with the European Union in 2011.

Economic reforms began in 2000 and in general strengthened economic activity for a nine-year period, facilitating GDP growth. Reforms worked to help increase living standards and real incomes, boost consumption and investment in the economy, housing and tourism, and bolster savings. The downside of the new economic policy was a sharp rise in external debt and faster growth in imports than exports. Growth was based on an increase in spending, which was largely financed by borrowing from international financial markets. It thus made Croatia extremely vulnerable to the global financial crisis begun in 2008. Since the last quarter of 2008 to the end of the review period in early 2013, GDP each quarter has fallen.

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

Since the end of the military occupation of Northern Dalmatia, Lika, Kordun, Banija and Western Slavonia and the peaceful reintegration of Eastern Slavonia and Baranya in 1998, the government has maintained control of the whole territory. There are no armed forces or criminal organizations that question the state's monopoly on power. Exiled political leaders of rebel Serb groups from the 1990s have tried to revive the idea of the continuity of a Serbian quasi-state on Croatian territory, but without success. As of the end of the review period, there are no actors in Croatia or abroad who question its sovereignty.

The preamble of the Croatian constitution defines the country as the nation-state of the Croatian people and all its citizens. Some ethnic Serbs have been dissatisfied with the language and meaning of this provision. Among Serbian political representatives, some continue to express dissatisfaction that Serbs have lost the constitutional status they previously held until 1990. During the Socialist Federal Republic of Yugoslavia, the Socialist Republic of Croatia was defined by the constitution as the national state of the Croatian people, the state of the Serbian people in Croatia and the state of other peoples and nationalities that live in it. Serbs, according to the 1991 census, accounted for 12.15% of the Croatian population; according to the 2011 census, however, Serbs accounted for 4.36%. The substantial decrease is a consequence of the war, as most Serbs were expelled or fled and have not returned, while others assimilated. Citizenship is acquired in Croatia by the principles of *ius soli*, *ius domicile* and *ius sanguinis*. Foreign nationals who consider themselves ethnic Croats or descendants of ethnic Croats (amounting to approximately half of Croatia's resident population) can more easily acquire Croatian citizenship than other foreign nationals, although there is no legal obstacle that would prevent any racial, linguistic, religious or other group from acquiring Croatian citizenship. All children born in Croatia acquire Croatian citizenship at birth if they have at least one parent who is already a Croatian citizen.

Question  
Score

Monopoly on the  
use of force  
10

State identity  
9

Croat citizens residing in Bosnia and other states are entitled to vote in parliamentary elections, and since the 2011 parliamentary elections, the number of their representatives has been limited to three.

The Catholic Church is the dominant religious community. According to the 2011 census, 86.28% of the population declares itself as Catholic. Although the constitution guarantees the separation of church and state, the church has a substantial impact on political life. Its representatives often make statements which emphasize Croatian national and religious values, or the threat of the country's communist heritage. Therefore, when making decisions regarding the relationship between church and state, the regulation of marriage, family relations or legal status of sexual minorities, authorities must count on clerical influence in shaping public opinion as well as the opinion of the political elite. This may have been the reason why Prime Minister Milanovic publicly announced that Croatia would not change its agreement with the Holy See. It is on the basis of the agreement that the state funds the church and secures other privileges, although the agreement also creates dissatisfaction for a part of the public. Despite its influence, the church fails to significantly impact policymaking within parliament (Sabor) and the executive branch. Policies that fall on the more socially liberal end of the spectrum, such as legislation regarding artificial insemination, have prompted the church's condemnation. But the government and a parliamentary majority regardless passed the measure into law in 2012. The church also objected to the new school curriculum on health education, specifically sections dealing with sexuality, sexual minorities, contraception and other issues, stressing that the government had no right to impose its "ideology" over schools, but instead stressed that parents should decide what sex education their children should receive. This caused a sharp reaction from the Croatian education minister, who called the church's attitude "medieval." Other religious communities in Croatia maintain a minor role in society, and their views on certain moral issues have almost no impact on political institutions and the legal system.

No interference of religious dogmas  
9

The administrative structure of Croatia is not as efficient as administration found in developed countries. Its ineffectiveness is the result of poor public policies, a lack of government control and a lack of sanctions over poor conduct. It is also result of not resolving long-standing administrative problems.

Basic administration  
10

## 2 | Political Participation

Regular parliamentary elections were held on 4 December 2011. After eight years of governing majorities led by the Croatian Democratic Union (HDZ), the elections were won by a coalition of four center-left parties led by the Social Democratic Party (SDP). The electoral process is administered by a permanent body, the State Election Commission (DIP), whose members are elected by the Supreme Court and parliament (Sabor). The president of the Supreme Court is ex officio chairman of the DIP. The

Free and fair elections  
9

elections were conducted in accordance with the principles of universal, free, secret and equal suffrage. Each voter has one vote in one of 10 multimember constituencies. Elections were free and fair according to international standards and there were no recorded cases of violence, theft of votes or other election irregularities. The only major problem that has emerged during elections is in relation to voter lists, which generally show a larger number of voters than there are citizens in Croatia. This has to do with the fact that there is a smaller percentage of people on the list who do not have permanent residence (or who have died) in Croatia. This is a problem as it presents opportunities for the manipulation of votes. Two groups of citizens have special status. Croatian citizens belonging to ethnic minorities have the right to choose whether they will vote for an electoral list in the electoral district where they belong according to their place of residence, or vote in the special 12th constituency for candidates of ethnic minorities. Croatian citizens who are not residents in the Republic of Croatia (diaspora) vote in a special 11th constituency.

In principle, there is no actor who has the right to veto the actions and decisions of democratically elected authorities. In practice, the army was one such actor yet has been depoliticized after many years. While the army was politicized in 1990s, President Mesić in 2000 forced several generals into early retirement because of their political activity. The clergy and business elites are only partially able to impose their views on government, but like other interest groups, they can influence laws and policymaking but cannot block the democratic electoral process. Some segments of the security and intelligence services remained loyal to the former government for months after the political change took place. Today, there are influential actors but no group or individual has de facto veto power.

The constitution guarantees freedom of assembly and association. There are restrictions on gatherings for security reasons, such as gatherings in the square in front of governmental and parliamentary buildings, but protests or gatherings of citizens in general are not prohibited and not discouraged. The constitution prohibits the foundation of political parties whose programs or activities are directed against the democratic order or threaten the existence of the Republic of Croatia, but this prohibition is not applied to political opponents.

There is constitutionally guaranteed freedom of expression in Croatia. The constitution expressly prohibits censorship, and journalists are guaranteed the right to freely report and access information. However, such freedoms still are a long-standing problem that while improving, still exists. Most notably, journalists at the public Croatian Radio Television (HRT) have accused some editors of enforcing censorship. The media in general shows a political bias, but most try to create at least the illusion of objective reporting. During the review period, there were several physical attacks on journalists and death threats. The government does not enforce censorship, and many electronic and print media outlets freely criticize the government and opposition voices. A scandal erupted at the end of 2012 when police

Effective power to govern

9

Association / assembly rights

10

Freedom of expression

7

director Oliver Grbic was accused in one newspaper that he had allegedly ordered the wiretapping of Chief State Attorney Mladen Bajic and eight journalists during the 2011 electoral campaign. The wiretapping was allegedly ordered because of information leaks in a criminal investigation of the ruling Croatian Democratic Union (HDZ) over the party's and its president's alleged corrupt relationship with Fimi, a media company. Internal controls ordered by the interior minister, Ranko Ostojic, found that there had been no wiretapping, but there were a few cases of the monitoring of journalists. In June 2012, the country's leading newspaper Vjesnik was closed because its owner, the government, failed to sell it to a foreign investor.

The freedom of expression is partially limited as the media space has effectively grown smaller, and at the same time has become more controlled by the few remaining media groups. The economic interest of media elites are more relevant than discreet methods of political influence.

### 3 | Rule of Law

The constitution divides political power between the legislative, executive and judiciary branches. Judges are appointed by the State Judicial Council, whose members are selected by parliament from the ranks of judges, university law professors and members of parliament. Judicial review is performed by the Constitutional Court, which in Croatia is not considered part of the judiciary branch. In practice, there is separation of powers, although parliament is still not able to hold the executive branch sufficiently accountable.

Separation of powers

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The independence and effectiveness of the judiciary have been one of the biggest issues in Croatia's accession to the European Union. Recent governments have tried to improve the situation, especially with regard to corruption issues, governmental interference and judiciary ineffectiveness, but each government was differently committed to the task. While Sanader's government (2003 – 2009) was deeply involved in issues of crime and corruption, the two governments since 2009 have devoted more attention to these issues. However, despite some progress, the judiciary is one of the reasons why Croatia, even after the completion of EU negotiations, will be under monitoring until its accession date. The Croatian Association of Judges sharply criticizes authorities on occasion over the state of the judiciary and governmental interference with judicial independence.

Independent judiciary

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In its 2012 monitoring report on Croatia, the European Commission noted that the self-governing bodies of the judiciary, the State Judicial Council and the State Prosecutorial Council, have lacked resources, have not systematically and accurately checked the asset declarations of judges and have been reluctant in applying disciplinary procedures in cases of wrongdoing by judicial officials. According to the



European Commission, the procedures of selecting and assigning new judges and prosecutors should be improved.

Croatia applies a continental European model of constitutional review of laws and other legal acts. Only the Constitutional Court has this right; regular courts do not. Some Constitutional Court decisions during the review period oppose the government and parliament in some important issues, such as the decision over the electoral law for ethnic minorities. In practice, judges are not influenced directly by politicians or other influential actors, but some decisions are shaped by the dominant social atmosphere, which is in turn largely shaped by the media. Croatia has quickly moved from practically no corruption cases to politicians being charged and sentenced on practically all counts raised by prosecutors.

In November 2012, in the first case of many brought against him, former Prime Minister Ivo Sanader was convicted of corruption and war profiteering and sentenced to 10 years in jail. During the review period, a former deputy prime minister and several directors of private and public companies were also convicted of corruption and other crimes and sentenced. The police and the judiciary have pursued investigations into corruption at universities, and at the end of 2012, officials announced leads in an investigation against some physicians. These proceedings, from 2009 to 2012, have changed the view that the country's political and economic elite can engage in corruption without risking prosecution or conviction. Influential elite groups have sought to bribe judges to change rulings. For example, after former Osijek-Baranya county official and member of parliament, Branimir Glavas, was sentenced to prison for war crimes against ethnic Serbs in Osijek in 1991 and 1992, his supporters tried to bribe Supreme Court judges to overturn the sentence. One of the people against whom the investigation was undertaken was a member of parliament from Glavas' party, Ivan Drmic. He was sentenced to one year probation after he entered a plea bargain with the state attorney's office. However, he did not abandon his political activities and ran in the 2011 parliamentary elections, winning again a seat in parliament. First Deputy Prime Minister Radimir Cacic in early 2011 was involved in a car accident in Hungary in which two people were killed. Having been sentenced by a Hungarian court in 2012, he did not resign from his government post, although many people believed that he should resign. After his release and his term was changed to an unconditional term of 11 months, Cacic resigned as deputy prime minister but delayed his resignation as party president.

Prosecution of  
office abuse

8

Civil rights in Croatia are protected by relevant legislation, and there are institutions that citizens can turn to over civil rights issues, such as ombudspersons, public prosecutors and the Constitutional Court. Some of these institutions are often ineffective; citizens can then turn to local human rights organizations and other civil society initiatives and in some cases, the European Court of Human Rights. Among

Civil rights

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these civil society initiatives there is a well-developed network of women's organizations that work systematically to combat discrimination against women.

Rights and freedoms are de jure strongly protected by the constitution and can only and exceptionally be restricted by law to protect the rights and freedoms of others, of public order, morality and health, or in the event of war, a large-scale natural disaster or imminent threat to the independence and integrity of the country. Provisions on the right to life, prohibition of torture, cruel or degrading treatment or punishment, the legal definitions of offenses and punishments, on freedom of thought, conscience and religion cannot be suspended. Perpetrators of crimes, including those against life and bodily integrity, are prosecuted by judicial authorities.

However, despite a good legal framework, in practice the actual state of human rights protections in Croatia is not high. In its 2012 monitoring report on Croatia, the European Commission noted that Croatia does not sufficiently protect minorities, in particular Croatian Serbs, against threats or acts of discrimination or violence. Although the situation has improved considerably, in many areas, especially within the family and at work, women often are not equal to men and are much more vulnerable to domestic violence and in general earn less than men. National minorities are guaranteed civil and political rights that are commonplace in liberal democracies, but in practice, some groups, especially Roma and Serbs, still face discrimination. While there is no legal discrimination against these groups, the exclusion of Roma from social, political and economic movements has created a vicious cycle of poverty, crime and poor education. In practice, members of the lesbian/gay/bisexual/transgender (LGBT) community also face discrimination, as do other vulnerable groups.

#### 4 | Stability of Democratic Institutions

With the introduction of a parliamentary system in 2000, a single executive, headed by the prime minister, formally replaced a dual executive system formed by the president and prime minister. In 2001, constitutional amendments abolished the second house of parliament, creating a unicameral parliamentary body. These changes spurred the consolidation of democracy and have in general proved successful. Consequently, the new system of government has not been reformed. The president, government and parliament are institutions which have been accepted by Croatian citizens and political elites. The candidate for Social Democratic Party (SDP), Ivo Josipovic, won the 2010 presidential elections, with the SDP winning the 2011 parliamentary elections. This created a situation where the president, the government and the parliamentary majority all, in general, were of the same political mindset and thus worked essentially conflict-free. Even before the 2011 elections, the president rarely clashed with the center-right government, and when he did, such conflicts were eventually overcome. However, there is inherent tension within the

Performance of  
democratic  
institutions

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system that could emerge amid future government structures in which there is an opposition party president. At the local level, the most obvious conflict is between the assembly and the mayor of Zagreb. These two institutions are directly elected in local elections, and the mayor is not accountable to the municipal assembly. Although the introduction of direct elections in 2009 was supposed to increase the democratic legitimacy of local government authorities, this has not happened in practice. The new system of local elections has created more tension at the local level, and needs to be amended.

There is no relevant party in Croatia that questions the legitimacy of democratically elected institutions. The Croatian Democratic Alliance of Slavonia and Baranja (HDSSB), a regional party based in Osijek, does not recognize as legitimate the war crimes trial against its founder, Branimir Glavas, as party leaders think that the trial was simply an act of political persecution by Prime Minister Sanader and the Croatian Democratic Union (HDZ) against Glavas. But even the HDSSB does not question the legitimacy of the political system. Other actors, such as the Catholic Church and trade unions, do not question the legitimacy of the country's democratic political system and electoral results, but sometimes do question the legitimacy of particular policies. The Catholic Church especially trends more politically right than left; a fact that was evident during elections, as certain candidates or parties received the support of the church, while more left-leaning parties were criticized on grounds of their supposed communist legacy.

However, there have been cases of more radical criticism of the political elite. In this context, the limitations of democratic institutions are recognized, but sometimes the institutions themselves are recognized as a source of problems. Criticisms have come from left-wing student organizations as well as from other civic organizations, along with calls for different forms of direct democracy and deliberative democracy. There is clearly a need for democratically founded institutions to become more democratic in practice, while the context of a prolonged economic recession provides a setting that is conducive to radical action of a different sort. If democratic institutions fail to adjust, there will be more and more space for radical action.

## 5 | Political and Social Integration

Most parliamentary parties in Croatia were founded in the early 1990s. With few exceptions, parties which were formed after this period have had little electoral success. The two largest parties, the Croatian Democratic Union (HDZ) and the Social Democratic Party (SDP), have alternated stints in government since 2000 and have formed coalition governments. Many voters strongly identify with a certain party, which is reflected in elections. If the ruling party loses an election, it is considered to be a result of voters withdrawing either their participation or their ballot for a related party, but not a result of voters switching to a rival party. The party

Commitment to  
democratic  
institutions

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Party system

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system as of 2012 has become polarized, while a political center has almost completely disappeared from parliament.

Party clientelism strongly marks Croatian politics and economics, but shows different intensities among political parties. Clientelism has mostly been present in the HDZ, which is closely tied to several organizations, especially church and veterans' associations, whose many members are HDZ supporters, and in turn benefit financially from state grants. Among beneficiaries are people who, during the privatization drive in the 1990s, amassed significant wealth due to their affiliation with the HDZ. The intensification of criminal prosecutions since 2009 and the party's falling out of government in 2011 have prevented a continuation of such clientelistic practices. Other parties share some of these problems but, due to the long reign of the HDZ, have less-developed clientelistic networks. Both of the main political parties have been losing support during the review period. While the SDP has failed to fulfill its supporters' expectations, the HDZ has been shaken by internal conflicts. As a result, the whole party system has lost legitimacy.

In the 2011 elections, right-wing extremist and populist parties won some 8.8% of the vote (including parties Croatian Pure Party of Rights-Ante Starcevic (HCSP), the Croatian Party of Rights (HSP) and the Croatian Democratic Congress of Slavonia and Baranja (HDSSB)) and eight of 151 seats (for the HSP and HDSSB) in parliament.

There is a number of interest groups and trade associations in Croatia, and some are notably active in society. Among the strongest are trade unions, with which the government regularly engages in dialog as part of Economic and Social Councils, but the standing of which in society is low and the influence of which can be circumvented when needed. The influence of interest groups in politics is different, but (although business elites are gaining ground) no group is so strong that it could impose its views on government or suppress the needs or desires of other groups.

Croatian citizens and political elites support the democratic political system. However, part of the elite and many citizens are dissatisfied with the performance of institutions in Croatia, especially political parties. Some of causes of that dissatisfaction include widespread corruption in government and the effects of the economic crisis that has lingered since the end of 2008. The president regularly receives higher approval ratings than does the government. In contrast, the prime minister and the entire government are regularly criticized by different interest and social groups, as these bodies, responsible for the formation of policies, are what affect citizens the most. In early 2011, in Zagreb and other major cities, protests were held against the government and the political elite; these protests were spontaneous and not organized by opposition parties. Protesters were questioning the poor functioning of the democratic political system, but also criticizing the political elites and institutions as such. The level of trust in institutions remains low (especially in

Interest groups  
8

Approval of  
democracy  
7

relation to political parties) and the democratic political culture of citizens grows slowly. As the economic recession continues, the voices of those who think that there is too much democracy in Croatia are being increasingly heard.

Volunteer organizations exist in Croatia to assist in addressing common social needs, but such organizations have not expanded significantly during the review period. A substantial number of voluntary and autonomous organizations covering cultural, environmental or social issues have been developed. A dual tendency toward volunteerism however can be observed. On the one hand, there are more self-organized groups being created around specific issues and interests to bring people together. Yet on the other, on a daily basis Croatian citizens are less inclined to show social solidarity. Trust among citizens is limited. As part of research conducted in 2012, some 82% of respondents said that “in relations with other people, one should be careful,” and only 15% said that “most people can be trusted.”

Social capital  
7

## II. Economic Transformation

### 6 | Level of Socioeconomic Development

In Croatia, there are no deep social cleavages that could polarize society or would require the introduction of elements of a consociational democracy. According to the 2011 census, more than 90% of the population is ethnic Croatians. Specific social groups such as the Roma do not face legal discrimination, but in reality are a marginalized group and subject to discrimination in practice. Social inequality and forms of social exclusion primarily stem from differences in gender, age, education and geographic region. Women, the elderly and the uneducated, as well as those living outside Zagreb, Istria and northwestern Croatia, have fewer chances of making a living above state average levels or finding a job to match their educational qualifications. These inequalities are in part historical, but primarily are the product of the country’s economic transformation and legacy of the war over the last 20 years. Older people, once they’ve lost a job yet are still too young to retire and collect a pension, find it difficult to regain employment. This is primarily a result of the economic crisis of the 1990s when many jobs were lost and new positions were not created. Croatian youth also have trouble finding a first job, even after completing their formal education. The consequences of this are emigration and steadily declining population, a situation that has been static over the past 10 years. During the review period the employment situation did not improve as a result of the economic crisis; still, more could have been done. According to a report of the Croatian central bank (HNB), unemployment between 2011 and 2012 increased.

Question  
Score

Socioeconomic  
barriers  
8

The economic crisis has adversely affected socioeconomic indicators in Croatia. Croatia's HDI in 2011 was high (0.796), ranking it among countries with very high human development. The country's risk-of-poverty rate has increased from 20.5% in 2010 to 21.1% in 2011. Although Croatia ranks high (27 out of 146 surveyed countries) on the Gender Inequality Index with a score of 0.170, the gender gap persists in several ways. Men continue to prevail in politics and in economics, where women much less frequently hold management positions, and their unemployment rate is higher. Women are more often exposed to domestic violence, receive a lower-than-average income than men and generally have to invest more effort in achieving an equal position in society. Nonetheless, women's status is improving. Women in recent years have occupied more government positions, for example. Jadranka Kosor was a former prime minister, while the government during the review period had several female ministers. In some areas, there are positive trends that equate the ratio of men and women in the same job or even show a larger proportion of women. For example, there is an increasing proportion of female professors in higher education, and every year more female students graduate than males. The prolonged economic recession however has increased poverty and inequality levels.

Economic indicators		2009	2010	2011	2012
GDP	\$ M	62244.2	58873.8	61789.2	<b>56441.6</b>
GDP growth	%	-6.9	-1.4	0.0	<b>-2.0</b>
Inflation (CPI)	%	2.4	1.0	2.3	<b>3.4</b>
Unemployment	%	9.1	11.8	13.4	-
Foreign direct investment	% of GDP	5.5	1.4	2.0	<b>2.3</b>
Export growth	%	-16.2	5.2	2.0	<b>0.4</b>
Import growth	%	-21.4	-1.4	1.2	<b>0.1</b>
Current account balance	\$ M	-3042.7	-847.5	-400.9	<b>-208.1</b>
Public debt	% of GDP	35.8	42.6	47.2	<b>56.3</b>
External debt	\$ M	-	-	-	-
Total debt service	\$ M	-	-	-	-

Economic indicators		2009	2010	2011	2012
Cash surplus or deficit	% of GDP	-3.1	-4.5	-4.7	-
Tax revenue	% of GDP	19.4	19.4	18.6	-
Government consumption	% of GDP	20.2	20.1	20.1	<b>19.9</b>
Public expnd. on edu.	% of GDP	4.4	4.3	-	-
Public expnd. on health	% of GDP	6.6	6.6	6.6	-
R&D expenditure	% of GDP	0.83	0.73	-	-
Military expenditure	% of GDP	1.8	1.7	1.8	<b>1.7</b>

Sources: The World Bank, World Development Indicators 2013 | International Monetary Fund (IMF), World Economic Outlook 2013 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2013.

## 7 | Organization of the Market and Competition

Despite the economic crisis, Croatia is still able to pay its international debts. During the review period there were no problems that could have forced the government to scrap its budget, but toward the end of 2012, the country's credit rating was lowered. In general, the state would be in better economic shape if effective reforms had been undertaken. The new government in 2012 launched a tax reform that was supposed to create a more efficient tax collection system and provide tax relief as well as create the conditions for renewed economic growth. The government also announced new investments, especially in the energy sector; these investments were to be undertaken by state-owned companies, yet at the end of 2012 it appeared that such investments were only partly realized. There is almost no administrative management of prices, with some exceptions, such as with petroleum products and natural gas. The government is working to liberalize the natural gas market, but faces problems. The price of energy for households is considered a social issue, and as a result prices remain unrealistically low. Croatia still struggles with bureaucratic barriers to foreign investment. As a result, many investments have fallen through and even foreign governments have addressed this problem on a state level. The One Stop Shop program of the Sanader government, which was aimed at reducing investment barriers, and the promise of ministers in the Milanovic government to personally review all investments exceeding a certain value, have not proved particularly successful. The problem resides not only with inertia of state administration but also with state-owned companies that are slow to respond to private investor calls for cooperation. However, this problem is well recognized and government administration is investing more effort to solve it.

Market-based  
competition  
8

Market competition in Croatia is regulated via the Market Competition Protection Act, as well as a number of bylaws. Croatia has incorporated anti-monopoly and anti-cartel provisions into its legislation. Since November 2010, the Croatian Competition Agency has been in charge of implementing leniency programs against cartels, following U.S., Canadian and EU models.

Anti-monopoly  
policy  
8

Croatia became a World Trade Organization member in 2000, while in 2001 it signed an agreement with the European Union that abolished all quota and quantitative limits on Croatian exports of industrial goods. When another agreement with the European Union came into effect in 2007, all quotas and quantitative limits were removed for exports from the European Union to Croatia. Croatia has an extremely negative foreign trade balance; the export-import ratio in 2010 was 58.8%, and in 2011 it was 58.9%. Bosnia and Herzegovina maintains a special status in international trade with Croatia, as the two countries share a long and in some parts poorly controlled border, making possible the smuggling of goods. This country is one of the few with which Croatia has a trade surplus.

Liberalization of  
foreign trade  
10

The global financial crisis so far has not deeply affected the business of larger Croatian banks. The Croatian banking system's performance has improved and has shown increased stability over a 10-year period. The Croatian central bank (HNB) works independently and has the mandate to set and implement monetary and exchange rate policy. Its independence is protected by the constitution and its influence has strengthened in recent years, with bank governors occasionally voicing dissenting opinions to those of the government. This dissent became especially marked since 2008 and the beginnings of the economic crisis, during which bank governors advocated a change in economic policy toward a reduction of public spending and the building of a stable foundation for economic recovery. Although Boris Vujcic became the new bank head in 2012, this change in leadership did not result in a radical shift in monetary policy. The new government began implementing public spending cutbacks in 2012, but Vujcic at the end of 2012 said reforms were not deep enough. After surviving two serious crises in the latter half of the 1990s, the Croatian banking system as of the review period is stable. All large banks are owned by foreign banks, and this has led to the adoption of corporate standards in the banking sector. The banking sector was also hit by the economic crisis, with the rate of nonperforming loans growing from 4.9% at the end of 2008 to 11.6% at the end of 2011. In the last four years, the capital adequacy ratio has grown from 15.2% in 2008, 16.4% in 2009, 18.8% in 2010 and 20.17% at the end of the first half of 2012. The situation however is still better than in neighboring countries, and some analysts credit the HNB for this. The HNB has also remained one of the few state institutions that have maintained a good reputation because of its work, despite harsh criticisms from some economists.

Banking system  
9



## 8 | Currency and Price Stability

Inflation in Croatia remained low in 2010 (1.1%) and 2011 (2.3%). An inflation spike in September 2012 was attributed by the central bank (HNB) to expected seasonal price increases. Croatia's currency, the kuna, is not linked to any foreign currency, though the euro is the most important foreign currency influencing foreign exchange policy. The kuna's exchange rate against the euro is stable, but varies considerably against the U.S. dollar and Swiss franc. Given that citizens' loans are usually tied to the euro (to a lesser extent to the Swiss franc), a strengthening euro (or franc) has significantly hampered loan payments. For years, some Croatian economists have advocated a more flexible exchange rate to mitigate the effects of what they consider to be a too strong kuna. A benefit of a weaker kuna would be more competitive exports, but a weaker kuna also makes it difficult for citizens to make loan payments to banks. At present, neither the government nor the HNB have sought to depreciate the kuna. Though Croatia is a member of the European Union, it will probably not be eligible to adopt the euro for a few years.

Anti-inflation /  
forex policy

9

In law and in practice, the HNB is independent of the government and responsible to parliament alone. Its power and prestige are a consequence of its consistent monetary and banking policies as well as the personal reputation of its former leadership. Boris Vujcic, the HNB's new head at the time of writing, continues to pursue the anti-inflationary policy of his predecessor and a stable exchange-rate policy against foreign currencies.

The government's fiscal and credit policies face many critics. In the review period the government of Prime Minister Milanovic has faced less criticism, however, than did the government of Prime Minister Kosor, but the policies of both governments have not been successful enough to pull country out of the crisis. In December 2012, the credit agency Standard & Poor's lowered the debt rating of Croatia to "junk," from BBB-/A3 to BB + / B. The main criticism was that the country has not made enough deep structural reforms, with concerns that Croatia may remain with such a rating for a longer period of time. The gross international reserves of Croatia in 2011 amounted to €1.195 billion, historically the country's largest reserve amount. Despite the foreign trade deficit, reserves have grown due to borrowing on international financial markets and foreign exchange revenue from summer tourism. External debt in late 2011 was €45.734 billion and accounted for 99.6% of GDP. It has decreased compared to 2010 by about €750 million. Public debt in 2011 amounted to 45.7% of GDP and was the highest to date. Such a state of national finances undermines macroeconomic stability as public spending is greater than revenue; there are no effective economic policies and unemployment is rising.

Macrostability

7

## 9 | Private Property

Croatia's constitution stipulates that entrepreneurial freedom and property rights can be limited in exceptional circumstances, related to the national interests and security of the Republic of Croatia, as well as the interest of the natural environment and human health. However, during the last 20 years, these rights and interests have been secured only partially because the Croatian Democratic Union (HDZ) political elite held an advantage during the privatization of previously publicly owned companies. During the period under review, such abuse has decreased significantly as criminal proceedings against top state officials have created too much risk for future perpetrators. The acquisition of private property in Croatia is allowed except where there is a risk of monopoly or cartel formation. Selling real estate to foreign nationals is limited, except for EU nationals, a situation which has in recent years been liberalized. This however was met with some controversy in Croatia, but the public outcry was not so significant that it would prevent the government from acting. In negotiations over EU accession, it was agreed that the selling of agricultural land to EU nationals would start seven years after the accession date, with the possibility of specific negotiations which would extend the ban for an additional three years. That ban has now been bypassed, so that foreigners cannot buy farmland directly but through the formation of a private company in Croatia, which then has the right to purchase land.

After abandoning the concept of social ownership in 1990, Croatia has sought to adopt the Western model governing private and public property. During the privatization process in the 1990s, there were numerous instances of illegal activities and political corruption. Consequently, the privatization process was unsuccessful in many cases, and the volume of economic activity reduced. Croatia in 2012 has not yet reached the level of industrial production it achieved in 1990. After the change of government in 2000, irregularities in privatization efforts were greatly reduced, although after 2003, Prime Minister Sanader was accused of involvement in corruption and other economic crimes. Only after his departure from the post in 2009 did the struggle against corruption intensify, and private ownership has become a less negative concept than was the case during the privatization era. The state has over the years reduced its equity stake in many companies, leaving only strategic industries in government hands, though further privatization is also being considered. This has caused public concern as many believe such actions are akin to "selling of the family silver." The government, however, believes that in some cases privatization is necessary, because private owners could be more successful managers, or out of sheer necessity in filling budget shortfalls. In 2012 the government put forward a proposal that the state-owned Croatian motorways be put to a concession at a price of €2 billion to €3 billion, a sum which would reduce the country's foreign debt.

Property rights  
9

Private enterprise  
8

## 10 | Welfare Regime

The Croatian social security system is largely public, financed through the state budget and local government budgets. A small share of the overall system is covered by other social organizations and the Catholic Church (through its humanitarian institutions). Social security covers unemployment benefits, benefits for maternity leave (and three months of paternity leave as well) and supports those who live below poverty level, Homeland War veterans, as well as supports the pension and health care systems. The two largest parts of the social security system – pensions and health – have been the source of problems for several years. All employed citizens of Croatia are legally obliged to pay contributions toward health and retirement insurance, but these contributions do not suffice in covering current health and pension expenses. The public health system covers universal basic health insurance, but the level of expenditures has put great pressure on the state budget. The public however would be sensitive to a reduction in health care services; Finance Minister Slavko Linic in December 2012, after Croatia’s credit rating downgrade to “junk” status, announced changes to the budget but without touching salaries and pensions. The introduction of patient participation fees was met with resistance, especially among the poor. Yet problems in the pension system started in the 1990s when a number of companies went bankrupt and many people went into early retirement. Since then, there has been an unfavorable ratio between the number of employed and the number of retirees, which as a consequence has led to a relative reduction in monthly retirement benefits as compared to the average monthly salary in Croatia. After 2000, the situation improved in that the average monthly retirement benefit grew, but overall, the mode of financing the pension system is unsustainable. The 2002 introduction of the second-pillar financing of pensions, which lead to the financing of a segment of the obligatory fee via private investment funds (in addition to the pay-as-you-go system), did not produce the intended results. During 2009 and 2010 there was much public debate over abolishing the second pillar, in essence nationalizing it. It was however not abandoned, probably because the move would mean yet another pension reform that would result in new charges.

Croatia in recent years has made advances in creating equal opportunities for its citizens in access to education, public services and employment. Women, ethnic and religious minorities are, generally speaking, neither legally nor in practice systematically disadvantaged in accessing services. One ethnic group that still suffers significant discrimination in access to public services and employment as well as education is the Roma population. All legal obstacles have been removed and a national program for the Roma was adopted in 2003. Croatia joined the Decade of Roma Inclusion 2005 – 2015. However, the Roma remain locked in a vicious circle of poverty, social exclusion and widespread prejudice. In terms of educational attainment, few Roma complete secondary school and rarely reach the tertiary level.

Social safety nets  
8

Equal opportunity  
8

Although some minor progress ought to be noted, the recent economic recession has slowed down the pace in practice.

After much debate, the Minister of Veterans' Affairs in December 2012 published a register of war veterans to facilitate the identification of persons who should benefit from state pensions but have not fought for Croatia in the wars associated with the breakup of the former Yugoslavia.

Finally, it is important to identify members of groups in Croatia that are significantly marginalized in society, such as people with learning disabilities, people with mental health problems, the disabled, individuals living with HIV/AIDS, sexual minorities and asylum seekers. These individuals sometimes do not have the same opportunities as their neighbors because of the persistence of prejudice in some institutions as well as on a wider societal level. However, positive developments in recent years are obvious following an increase in public awareness. This especially applies to sexual minorities that can more freely express their sexual orientation in society than previously. In 2011 the country's first gay pride parade was held in the city of Split; another parade was held in 2012. At the first event, participants were subjected to insults and physical attacks; in 2012, the event was peaceful.

## 11 | Economic Performance

After nine consecutive years of GDP growth, the global financial crisis hit Croatia in 2008. The biggest drop in GDP was -6.9% in 2009. In 2011, growth was 0%, and in 2012 GDP growth fell again. The decline was expected as a result of government-implemented economic reforms. The government has announced that an economic recovery is expected in 2013, but rating agency Standard & Poor's, at the end of 2012, expressed skepticism in the forecasts of GDP growth of 1.8% for 2013. Following GDP growth rates of 0.6% and 0.8% in the second and third quarter of 2011 respectively, GDP at the end of the year started to fall again, and this trend has continued through 2012, with significant disappointment in the third quarter. Although this is the peak tourist season and usually reflects the highest growth numbers, GDP in the third quarter of 2012 fell 1.9%, as strong tourist revenue couldn't bolster the other flagging segments of the economy.

According to HNB data, GDP in 2011 amounted to €45.897 billion, the average annual rate of inflation (CPI) was 2.3%, the current account balance was -1.0% of GDP and public debt was 45.7% of GDP. The unemployment rate for the population older than 15 years was 13.5%, and the employment rate of the population aged 15 years and older was 39.5% (also 2011 figures). The employment rate is thus worse than in 2001, when unemployment was considered a chronic problem of the Croatian economy. Rising unemployment has continued in 2012 as a result of job losses and weak job creation. In Croatia, there are cyclical rises and falls of unemployment

Output strength  
6

which always falls during the summer tourist season, but summer unemployment in 2012 was higher than in the same period in 2011.

## 12 | Sustainability

The Environmental Performance Index 2012 score for Croatia is 64.16, and the country is ranked 20th out of 132 surveyed countries. As a result of education, the influence of non-governmental organizations and the requirements of international organizations and the European Union, public awareness on environmental issues has strengthened over time. One of the biggest problems is landfills, many of which do not meet international standards. Another problem is the regulation of rivers, conducted by a public institution called Croatian Waters. Some planned or already implemented projects have faced harsh criticism by Croatian and international experts over concerns of potential environmental harm. A further environmental problem has to do with the development of energy sector. For years there has been a plan to build a new coal-fired block in the power plant Plomin, in Istria. The local community and some environmental groups oppose coal as a fuel, but the new government insists on its use instead of gas, because of the price difference. A similar issue arose in the Dubrovnik region due to the construction of a hydroelectric power station, which was suspected to affect an entire ecosystem. In the context of the prolonged economic crisis, there is a realistic fear that environmental standards will be subordinated to the imperative to attract investments that would finally provide economic stimulus.

Environmental  
policy  
8

Over the last two decades, the need for education reform has been periodically mentioned, but by 2012 there still was no significant changes made to primary and secondary education. Since 2005 the so-called Bologna process has been implemented at universities, and it has brought about significant structural changes in higher education. Further reforms have been announced, but changes are slow and restrained by a lack of financial resources and bureaucratic slowness. Most primary and secondary schools are publically run and demand no tuition. There are seven public universities and one university run by the Catholic Church. Most undergraduate and graduate students are exempted from the costs of studying. There are also a number of private higher education institutions, mostly business schools, which require tuition fees. From 2007 to 2011, the number of graduates increased from about 21,000 to about 36,000 per year. According to Eurostat, Croatia in 2010 spent 0.7% of GDP on research and development. Public spending on education was 4.4% of GDP in 2009 (World Development Indicators).

Education policy /  
R&D  
8

# Transformation Management

## I. Level of Difficulty

In the triple transition (democratic, economic and state-building), Croatia has had a number of structural problems that have slowed down the transition process. They refer to the war and its ravaging effect, the occupation of a part of the national territory, legislation inherited from the communist era, large defense allocations, a sharp decline in economic activity and living standard, an inefficient judiciary, the growth of unemployment and the unfavorable number of retirees relative to the number of employees. During the time, these structural problems have disappeared or have been reduced. Another significant group of structural problems also has its roots in the 1990s. This is a large number of retirees, veterans and unemployed people.

Structural  
constraints  
2

Besides the drought which often occurs during the summer season in rural regions, Croatia is not affected by large-scale natural disasters. The number of HIV/AIDS cases in Croatia is very small, about 800 in 2012. The labor force is relatively well educated and only a small percentage of the population has only completed primary school. Road infrastructure is among the most developed in Central and Eastern Europe, but the problem of railways and railway infrastructure was not seriously addressed until 2012. One of the major structural constraints to the development of infrastructure is the geographical shape of the country that requires a great length of road network in relation to the country's territory.

Yugoslavia was considered as one of the most liberal countries in the communist world, and Croatia, after Slovenia was the most developed federal units in Yugoslavia. Like other communist countries Yugoslavia sought to provide support for the regime through mass participation of citizens in the regime's organizations, but as a result of the higher level of civil rights and freedoms, there were also informal groups that have operated freely. Yugoslav citizens were free to travel abroad, working as temporary workers in Western European countries and bringing information and ideas from these countries to Yugoslavia. Therefore, after the beginning of the democratic transition in Croatia, there was a bigger human capacity and knowledge of how to organize civil society than in most other post-communist countries. The war and hybrid political regime in the 1990s complicated the development of civil society, but after 2000 civil society has been strengthening and

Civil society  
traditions  
4

it influences the formation of public opinion and the actions of the political elite. NGOs grow and have become more prominent. They are usually present at public hearings on certain social issues, and even launch protest actions. Among the broader population the level of social trust and consequently social capital, however, remains rather limited.

The 2011 Census showed that Croatia is an ethnically quite homogeneous country. Over 90% of the population are ethnic Croats and over 83% are Catholics. Atheists are the second largest group, and the Orthodox third. In Croatia, there are no deep social cleavages that confront society and influence the political process in a manner that would lead to violence. There is an ethnopolitical cleavage between the ethnic Croat majority and the Serb minority, especially in the region of Eastern Slavonia. Part of the population in some Croatian regions shows disappointment towards the center, but the gap is bigger in relation to politicians and other members of the social elite from Zagreb than on the level of average citizens. In the 1990s, there was a sharp cleavage between ethnic Croats and ethnic Serbs, but since the end of war it has decreased. It continues to exist in regions where there is a large Serb population, like Vukovar. In Vukovar there are separate kindergartens, schools and coffee shops for ethnic Croats and ethnic Serbs. Such division of the town is not the result of official state policy, but is rather caused by nationalistic political representatives from both communities who rely on this division, on some veterans organizations as well as on the tendency of local ethnic groups to continue to function within their own ethnic communities, distrusting the other in a collective manner. Such informal division is often criticized by many political and non-governmental organizations, but also accepted as a reality caused by the devastating war in this region. There is no political violence in the country and occasional verbal outbursts of radical right no longer have a significant following.

Conflict intensity  
2

## II. Management Performance

### 14 | Steering Capability

The declared aims of governments since 1990 were the establishment of a democratic political system and market economy, proclamation of independence and joining the Western military and political organizations. During the nineties there was a period of regression but now over two decades later nearly all the main goals have been achieved and the last should be the entry to the EU. All other goals were of less importance relating to these, including prioritizing economic and social issues more. The implementation of the declared priorities was met with a number of difficulties and governments often had no clear idea about what to do or how to solve certain

Question  
Score

Prioritization  
8

problems. They had neither the capacity to do it because they did not have enough policy experts and outside experts were not consulted. For example, no government had clear vision of how to solve the problems of unemployment, adverse balance of foreign trade or an increase in external debt. Kosor's government did not dare to make sharp cuts in public spending in the budget rebalance in the autumn of 2010 and thus avoided necessary reforms in order to address the crisis. It has become especially apparent in the last year of its term, which was an election year. Milanovic's government tried to change this trend but after the expiration of the first year of its mandate it had to admit that in many areas it failed. This is primarily related to the reduction of the budget deficit, unemployment and the reform of state administration as well as the beginning of economic recovery more broadly. It has not used its first year of the term for the widespread introduction of unpopular measures, which were limited in character. Layoffs in state-owned companies were announced in order to increase their efficiency, but at the same time state administration remained intact.

The government has limited success in implementing its policies. The problems in their implementation are structural difficulties that have roots in the past and the government's lack of commitment to overcome the difficulties in the implementation of its policies. This primarily refers to the resistance of various social and interest groups whose interests were affected by some government policies. Some trade unions strongly opposed the government's plan in 2012 to reduce employee benefits in certain public services in order to reduce public expenditure. An additional problem is the mismatch between ministers, especially if they come from different parties. In the first half of 2012 the First Deputy Prime Minister Radimir Cacic of the HNS and the Minister of Environmental Protection Mirela Holy of the SDP came into conflict because of the construction of hydropower plants near Dubrovnik for which there were doubts that it will harm local ecosystem. The problems also arise if the government and local authorities have a different attitude about an issue, such as the construction of coal power plants in Istria. These problems can result in temporary or even permanent halt of controversial projects.

The Milanovic government in 2012 started some reforms that were supposed to balance public spending and create a more efficient economy, drawing lessons from the failed fiscal and economic policies of its predecessors. These reforms are driven by the country's needs, but also by lessons learned from the failures of past economic policies. The government has demonstrated itself to be somewhat more open to public discussions and consultative processes in which policy proposals and existing policies can be scrutinized, adjusted or substantively changed.

Implementation  
8

Policy learning  
7



## 15 | Resource Efficiency

Croatia's public administration is oversized and inefficient, and it has grown, not shrunk, over the past 10 years. No government, not even the government during the review period, has dared to cut back on public service employees, for fear of a negative public reaction at a time when Croatia continues to struggle with high unemployment. Political patronage and nepotism are widely practiced in the public sector. In the process of hiring for public administration or institutions, there are many cases in which tenders are crafted to suit a particular candidate, or in which a state official intervenes to do so. One famous case of official intervention came in 2012, when Minister Mirela Holy allegedly used her position to help a friend get hired; the result of which was when the issue came to light, Holy resigned. The state budget for years has booked higher expenditures than revenues. The budget deficit is financed by government borrowing, which increases public debt. Budget planning is however more transparent than it was in the 1990s when, for example, budget items earmarked for the Ministry of Defense were not clearly stated, which opened up the possibility of non-transparent spending. Public institutions and state-owned companies are legally obliged to carry out tenders for procurements valued more than the legally prescribed maximum to avoid the possibility of corruption and to more effectively spend funds for these purposes. Nevertheless, the State Audit Office and the courts have dealt with cases in which this rule is violated. Such problems also exist at the local government level. The reform of 1993, which revised the organization of municipalities from a hundred to over 500 cities and municipalities, divided into 20 counties, has been criticized as misguided. Over the years, the number of cities and municipalities has been further increased. The multiplication of local governments is considered as one reason in the reduced effectiveness of local government and reforms. Despite recent reforms, the running of local government remains expensive, and revenue from small towns and municipalities is insufficient for their sustainability without help from the state central budget.

The government still fails to effectively charge applicable taxes. After the government handover in late 2011, the new finance minister launched tax reform geared to enable a more efficient collection of taxes and tax assuagement for the economy. The reforms would also introduce new taxes, such as taxes on real estate ownership. The problem of public health financing is one of the most difficult public service financing questions in Croatia. Hospital debts are measured in hundreds of millions of euros, while the public is still not satisfied with the quality of services.

There were conflicting objectives between different public policies in 2011 and 2012. For example, clashes over the need for economic development while maintaining environmental protections; a decrease in unemployment numbers while state-owned companies moved to cut unnecessary workers; strengthening the effectiveness of the

Efficient use of  
assets

7

Policy  
coordination

6

system of public education while simultaneously decreasing education expenditures. These problems have proved challenging to the government that even amid an economic crisis, must achieve several goals simultaneously. The Milanovic government in particular had to manage a number of conflicts between ministers of different political parties. Though not common, conflicts such as those between the First Vice-Prime Minister Cacic and Minister Holy or between the Finance Minister Slavko Linic and cabinet members from the HNS over the introduction of a new tax on real estate, are not resolved by the prime minister, who lacks both the will and authority to do so.

Due to a more efficient fight against corruption since 2009, public awareness of corruption's penetration into society has been increased. This has resulted in the intensive supervision over the spending of funds in public institutions, though such monitoring in many cases is still ineffective. Some public company directors, for example, some of whom are struggling financially and have poorly performing businesses, have tried instead to maximize their own material gain by buying expensive company cars for their personal use. Several such scandals in 2012 inspired a public outcry, forcing some government ministers to intervene and prohibit such ethically questionable business procurement. Another problem is the funding of political parties. Parliamentary parties are financed from the state budget according to the number of seats each has in parliament, yet attempts toward tighter legal controls have failed. Conflict of interest is another hot point. When entering public office, each official is obliged to leave any other private sector positions (such as business ownership), if they exist, and report all assets. Such a legal obligation has existed since the 1990s, but is criticized as the law does not outline sanctions for violators. The only way to penalize an offender is by releasing information publically, with the goal of exposing the individual to public condemnation, or force the individual to resign their position. Aside from the case of Mirela Holy, the environmental minister who tried to protect the wife of a fellow party member from dismissal, another public case revealed in December that Tihomir Jakovina, the government agricultural minister, owned an agricultural store. He retained his management position there he became a mayor in 2005 and a minister in 2011. The public however did not see this as a huge scandal, as it was simply considered a case of a minister ignoring his legal obligations (but not financially gaining by doing so), as opposed to the much more severe cases of conflict of interest of previous years. These cases do show however that public and media access to information over the functioning of public administration and government is crucial, and that public opinion cannot be influenced by the government through its repression of journalists.

Anti-corruption  
policy  
8

## 16 | Consensus-Building

Democracy was firmly established in Croatia after the change of government in 2000. While a democratic governmental structure was adopted at the beginning of the country's transition in the 1990s, the understanding of such a system by subsequent Croatian governments was not exactly in accordance with the prevailing attitudes in Western democracies. After the party's return to power in 2003, the Croatian Democratic Union (HDZ) abandoned its previous practice of controlling the media (at least for the most part), and fears of the international community that Croatia might return to less-democratic practices as in the 1990s proved unfounded. The extremist right-wing party Croatian Party of Rights (HSP) reformed itself and abandoned the legacy of the country's fascist Ustasha regime during World War II as a "failed ideology." Except for seven deputies from extremist right-wing parties, no parliamentary party in Croatia's parliament holds extremist political views. Right-wing parties accept the political views of the Catholic Church, but much of the public believes this is not inspired by the party leadership's religious beliefs but out of pragmatism, to maintain their influence among the religious electorate. There is a similar basic consensus of relevant actors on the acceptance of a market economy, but with greater deviations. For example, a surprise amid parliamentary elections during the review period was the performance of the Croatian Labor Party, a political party that participated for the first time in parliamentary elections and won six seats. It is on an ideological scale more leftist than the ruling Social Democratic Party (SDP), but it does not hold extreme leftist views. Trade unions represent a harder position in negotiations with the government and oppose amendments to the labor law which would, due to the opening up of employment possibilities, reduce workers' rights. In the current setting of a prolonged economic recession, the voices of those who question the value of a democratic political system (usually from the right) or those who criticize the inequalities created by a market economy (from the left) are heard more often.

There are several extremist right-wing and populist right-wing parties in Croatia; in the December 2011 parliamentary elections, three of the parties, the Croatian Party of Rights (HSP), the Croatian Democratic Alliance of Slavonia and Baranja (HDSSB) and the Croatian Pure Party of Rights-Ante Starcevic (HCSP) jointly won nearly 9% of the vote. These parties are embedded in a larger social milieu that is susceptible and accommodating to extremist right-wing nationalist attitudes and positions, as was indicated by mass demonstrations to celebrate the acquittal of Croatian war heroes in 2012 or the tens of thousands of fans who support the Croatian music group Thompson, criticized of glorifying Croatia's fascist Ustasha regime active during the World War II in their song lyrics. Right-wing and conservative parties and groups have protested against gay pride events or have opposed the

Consensus on goals  
10

Anti-democratic  
actors  
9

introduction of bilingualism in areas where an ethnic Serb minority lives, but in general, such groups have limited power and influence on the public at large.

Due to the high degree of religious and ethnic homogeneity in Croatia, and an absence of historical conflicts between regions and between the center and the periphery, the political leadership has no problem in overcoming conflicts that originate from social cleavages. One lingering problem is relations with Croatia's ethnic Serb minority and minority Orthodox religious community. In recent years, governments have pursued a policy of reconciliation and cooperation with the Serbian community. Such efforts are partly reflected in the coalition of the Croatian Democratic Union (HDZ) with the most influential Serbian political party in Croatia, the Independent Democratic Serb Party (SDSS). In this context, it can be said that the political leadership has not allowed conflicts based on ethnic cleavages to escalate, but at the same time, has pursued policies that effectively consolidated the cleavage in some areas. On the regional level, two political parties are advocating for greater government decentralization, but one of them, the Croatian Democratic Congress of Slavonia and Baranja (HDSSB, a right-wing nationalist party established after the expulsion of Branimir Glavas from the HDZ in 2005) does not seek to topple the unitary structure of the state. Neither former nor current Croatian governments at the time of writing have cooperated with the HDSSB.

The prime minister and cabinet members frequently meet with representatives of NGOs and social organizations, such as trade unions, employers' associations, churches, veterans' organizations and so on. As media freedom grows and the number of media outlets increase, so too does the impact of public opinion on government actions. The government therefore can no longer avoid the views and interests of civil society in the formulation and implementation of policies, although the state is still strong enough to resist interests that are seen as being contrary to the government's program and/or interests. This is especially true for the government during the review period, in its resistance to pressure from veterans' organizations not to publish a register of war veterans, or pressure from the church not to change the law on artificial insemination or not to introduce a unique program of health education in schools. Three previous HDZ-led governments succumbed to pressure, however, as they sought to keep the support of the electorate that stood by these organizations.

The legacy of war from 1991 to 2001 remains a historical burden for all the countries of the former Yugoslavia. Croatia's burden can be traced back to World War II, when the country was sharply divided into two political and military camps. Although the constitution of 1990 explicitly proclaims that the modern Croatian state is based on the legacy of the anti-fascist struggle in World War II, to date there are political forces that consider the defeat in 1945 as a disaster for the Croatian nation, and maintain a view toward historical revisionism. By 2012 these divisions have softened, but the wars in Croatia from 1991 to 1995 resulted in consequences for Croatian and Serbian

Cleavage /  
conflict  
management

8

Civil society  
participation

7

Reconciliation

8

relations, both between Croatia and Serbia as nations and between Croatian and Serbian people living in Croatia. Since the end of the war in 1995, conditions have improved and negative feelings on both sides have decreased. However, from time to time certain events stoke these dying fires. In November 2012, the International Criminal Tribunal for the former Yugoslavia (ICTY) acquitted two wartime Croatian army generals, Ante Gotovina and Mladen Markac, as the court was unable to prove their responsibility in organizing a “joint criminal enterprise” of ethnically cleansing Serb-populated areas of Croatia. Citizens and politicians in Croatia have welcomed and viewed this ruling as confirming Croatia’s status as an innocent victim of Serbian aggression. The ruling has had a detrimental effect for interethnic reconciliation in and beyond Croatia, since it has strengthened those who refuse to accept any Croatian responsibility for the wars of the 1990s.

Although the Croatian political leadership, past and present, has condemned individual crimes committed in the 1995 Operation Storm against Serbian civilians, the Croatian judiciary over the past 17 years launched investigations and sentenced only a small sample of perpetrators. Another lingering problem is the fate of 200,000 ethnic Serbs from northern Dalmatia, Lika, Kordun and Banija that fled their homes during Operation Storm in August 1995. Many of these people never returned to their homes and are still in Serbia or are dispersed throughout the world.

## 17 | International Cooperation

Political elites and public opinion in Croatia perceive the conditions and rewards established by the European Union and the United States as externally imposed pressure. Compliance with these conditions has therefore not been primarily motivated by intrinsic convictions but by cost-benefit considerations. Only a small part of the political elite has carried out suggested changes because of a commitment to democracy. In one way or the other, progress has been made and Croatia has thus separated itself from the other countries of the former Yugoslavia, where there exists still a profound instability of political systems and a lack of democratic consolidation. As a result, Croatia was in 2009 accepted as a member of the North Atlantic Treaty Organization (NATO) and in July 2013 is expected to become a member of the European Union. However, because of all the problems faced by the country over the last two decades and due to recent negative experiences with some new EU members, Croatia will be scrutinized under a monitoring mechanism until accession.

Effective use of support  
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Croatia has demonstrated its ability to meet the expectations of the European Union as part of its accession process. However, certain promises that were given by Croatian authorities have not been fulfilled, or are slowly being fulfilled. Examples include a slow march toward fighting corruption, judicial reforms and armed forces reform. Although authorities have repeatedly assured EU officials that an anti-corruption effort was underway, the indictment against former Prime Minister Ivo

Credibility  
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Sanader for his role in several corruption scandals was raised only in late 2010. Another significant issue is the administrative barriers for foreign investors that have still yet to be removed, the result of which is Croatia is seen as an unattractive investment destination. The rating agency Standard and Poor's downgraded Croatia's credit rating to "junk" level (BB+) in December 2012, indicating the declining trust of international financial markets in Croatia's sovereign bonds.

The Croatian political leadership supports reconciliation in the former Yugoslavia and cooperation among countries in the region. Relations with neighboring countries are particularly important. Although relations had improved over the years, the relationship between Croatia and Serbia was upset in 2012. After the presidential victory of the former extremist right-wing candidate Tomislav Nikolic in Serbia, the relatively frequent meetings of the Croatian president and prime minister with Serbian President Tadic stopped. Croatian President Josipovic refused to meet Nikolic as the latter had said that Vukovar, a Slavonian town shelled by Serb artillery in 1991, was a Serbian town. There are also other problems that have burdened the relationship between the two countries, such as the ethnic Serbian refugees from Croatia in the early 1990s and Croatia's recognition of the independence of Kosovo in 2008. Croatia also has unresolved issues with Slovenia. The first is related to a portion of the country's maritime and land border with Slovenia, following its demands for direct access to the open sea. Another dispute is related to Croatian citizens' savings held in Slovenia's Ljubljanska Banka (LB) that were not reimbursed to those who had not applied for compensation by the government of Croatia. In March 2013, Croatia and Slovenia agreed to withdraw the Croatian lawsuits against LB and to settle the problem through intergovernmental negotiations. Bosnia and Herzegovina maintains a special status in Croatian relations. This status stems from the lengthy geographical border between the two countries, the constituent status of ethnic Croats in Bosnia and Herzegovina and the legacy of the war of the 1990s. The present-day relations between two countries are improved and Croatia is no longer accused of interfering with the internal affairs of Bosnia and Herzegovina. Croatia supports the inclusion of all countries of Southeast Europe into the North Atlantic Treaty Organization (NATO) and the European Union and has set no formal barrier that would prevent this, despite undetermined land borders with Serbia and Bosnia and Herzegovina.

Regional  
cooperation  
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## Strategic Outlook

After its first year in office, the Croatian government during the review period was not able to set a solid foundation for the country's economic growth. Predictions for 2013 and 2014 include minimal GDP growth. To stimulate economic activity, the government, among other things, should simplify the administrative process for domestic and foreign investments and should reform public administration. Since the government has three more years in office at the time of writing, it may be expected to put in place some publicly unpopular measures to achieve these goals. The government however has put forward no serious plans, but instead turned its attention to economic investments in state-owned companies and a reform of the tax system. These measures cannot be considered effective until the implementation of profound structural reforms that would include the reform of public administration, enhancing the efficiency of the judiciary and, as a long-term aim, improvement of the education system on all levels. The general opinion is that public administration is not efficient and is overstaffed. Public education could be improved by increasing funding and finally adopting and implementing new educational programs. In the past two decades, reforms have been announced several times, but with exception of higher education, no serious steps have taken place. Changes should also include increased funding of scientific research, levels of which are currently lower in Croatia than the EU average.

Croatia's foreign policy has been dogged by poor relations with its neighbors. In recent years Croatia's biggest problem was relations with Slovenia, which in early 2013 refused to ratify the treaty over Croatian accession to the European Union because of unresolved issues dating back to 1991 and the collapse of Yugoslavia. Another problem exists with relations with Serbia, after President Nikolic and Prime Minister Dacic assumed power. In mid-January 2013, Prime Ministers Milanovic and Dacic met in the Serbian capital Belgrade, but the general impression was that the meeting took place under pressure from Brussels.

Although the poor socioeconomic status and non-consolidated political systems existent in most of Croatia's neighboring countries make them less than ready for EU integration, Croatia is expected to have a more active role in their EU accession process. The Croatian government after 1 July 2013 should avoid however connecting the requirement of solving bilateral problems with assistance to these countries in terms of EU accession. Assistance to neighboring countries could be the most efficient contribution of Croatia for their socioeconomic and political improvement. Because of the better socioeconomic and political situation in Croatia and its greater experience in negotiating with the European Union, it has the capacity for this sort of active regional foreign policy.