

# The World Bank in Croatia Country Snapshot



An overview of the World Bank's work in Croatia

April 2020

CROATIA	2019
Population, million	4.1
GDP, current US\$ billion	60.4
GDP per capita, current US\$	14,914
Life Expectancy at birth, years	77.8

## At a Glance

- Following positive developments in 2019, the coronavirus crisis is expected to cause a recession in Croatia in 2020, exacerbated by the country's heavy reliance on tourism.
- It is expected that disruptions will be short lived and economic activity will start to recover in 2021.
- Croatia is also dealing with the damage caused by the earthquake that struck the capital city Zagreb and its surroundings on March 22, 2020.
- The World Bank is working closely with Croatian authorities to support the Government and the Croatian people during these difficult times.

## Country Context

Since the beginning of 2020, the escalation of the COVID-19 crisis in Europe and the measures introduced by public health authorities to limit the contagion's spread have led to a rapid decline in economic activity.

Uncertainties surrounding the global—and the country's—outlook are substantial, and risks are tilted to the downside. A further adverse effect on world trade and on Croatia's GDP are to be expected if the lockdown is prolonged and trade restriction measures due to COVID-19 continue over a long period of time.

Lengthy disruptions in global supply chains and falling demand, especially for travel and tourism—the single most important sector in the Croatian economy—could contribute to an even stronger economic recession. This would also result in a further widening of the fiscal deficit, requiring substantial borrowing and leading to a large increase in public debt.

The social and economic impact of the coronavirus pandemic is further exacerbated by the damaging earthquake that struck the Croatian capital and its surroundings on March 22, 2020. While the results of the damage assessment are still pending, the economic impact is expected to be very severe and reconstruction may take several years.

It is anticipated that Croatia will need to revisit its growth model and focus on specific policies to increase its resilience to exogenous shocks and raise the economy's growth potential.

## The World Bank and Croatia

The World Bank has been a partner to Croatia for over 26 years. During this period, the Bank has supported more than 50 projects, amounting to about US\$3.5 billion, produced numerous studies, and provided technical assistance to help strengthen institutions and support the design of policies and strategies.

In May 2019, a new joint strategy for Croatia, the Country Partnership Framework (CPF) 2019–24, was approved, defining the Bank's engagement in the country over the next five years.

The new strategy is supporting Croatia on its path toward an inclusive society where communities, businesses, and regions can prosper for the benefit of all Croatians; where public institutions provide effective and efficient services; and where Croatia's rich natural capital is preserved and used in a sustainable manner.

### Key Engagement

The World Bank's current program includes two large operations in the transport sector. The Bank is working with the Ministry of Sea, Transport and Infrastructure on implementing projects in support of the restructuring of public roads and railway companies to make them more competitive and financially less reliant on state subsidies and thus less of a fiscal burden.

World Bank activities in Croatia also involve improving the business environment in several areas, including modernizing land registration; promoting entrepreneurship by simplifying the business registration process; and reducing the bureaucratic requirements for starting a business.

In addition, a new operation was approved at the end of March 2020 aimed at improving business regulatory procedures and judicial service standards for businesses and citizens.

### WORLD BANK PORTFOLIO

No. of Projects: 5

Lending: \$391.1 million

23 ongoing knowledge activities, including studies, technical assistance, and Reimbursable Advisory Services

As innovation is an important part of economic competitiveness, the Bank is financing research and development projects for innovative companies and researchers while also connecting public research institutions with businesses.

The Bank is working closely with the Ministry of Regional Development and European Union (EU) funds to establish a strategic planning system and to prepare the National Development Strategy (NDS) - Croatia 2030.

The Bank is helping the authorities to identify growth opportunities in the less well-off regions of Slavonia, Baranja, and Srijem to enable the Government to use EU funds more effectively and improve the welfare of the people in these areas.

The Bank is also providing advisory support to the Ministry of Agriculture in the formulation of a National Agriculture and Rural Development Strategy, as well as a multi-annual fisheries development plan for the post-2020 period of the Common Agricultural Policy (CAP) and Common Fisheries Policy (CFP) of the EU.

## Recent Economic Developments

The escalation of the coronavirus crisis and the measures introduced by public health authorities to limit the spread of the contagion have led to a significant decline in economic activity. The Government has prepared a package of temporary measures, potentially reaching 15 percent of GDP, intended to mitigate the negative effects of the COVID-19 crisis on the economy.

The package includes, inter alia, forgiveness or deferral of income and profit taxes, social security contributions for three months, a subsidy to employers for retaining their workforce, and a moratorium on loan payments to development and commercial banks.

In an effort to contain depreciation pressures, the Croatian National Bank intervened on the foreign exchange market to sell, for the first time in four years, €2.2 billion to commercial banks.

These events follow positive developments in 2019, when GDP growth accelerated to 2.9 percent from 2.7 percent a year earlier. Personal consumption continued to increase, supported by favorable labor market developments, an increase in consumer optimism, and further tax reductions.

The rise in public investment, estimated at 14 percent, largely reflected the rising uptake of EU funds.

Fiscal developments remained favorable, with public debt declining to 73.2 percent of GDP in the course of 2019. Labor market outcomes also improved further in 2019, with the unemployment rate dropping to below 7 percent.

## Economic Outlook

After finally reaching the pre-2008 level of output in 2019, Croatia is set for a deep recession. The coronavirus pandemic has resulted in a lockdown in many countries around the globe and might reduce Croatia's GDP by -6.2 percent this year. The country's tourism and exports of goods are expected to be severely affected, given the widespread travel bans and slowing activity in all major trading partners.

Repercussions for the labor market could be grave, with the unemployment rate rising to above 9 percent in 2020. The Government's intervention package will help in mitigating the downturn, though at the expense of a high budget deficit and a significant rise in public debt. It is expected that Croatia might record a fiscal deficit in 2020 of close to 8 percent of GDP.

The downward trajectory of government debt will be temporarily reversed, and by the end of the year, debt could reach almost 84 percent of GDP. It is assumed that the pandemic crisis will gradually fade by the end of the first half of 2020, which could lead to an economic recovery in the following years.

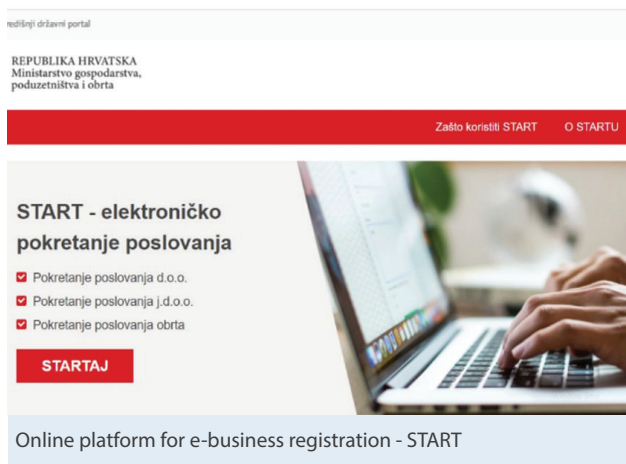
The fiscal deficit is expected to narrow in the next two years as expansionary measures unwind and growth picks up, but without additional consolidation, it could remain high.

Poor households are expected to be disproportionately affected by the pandemic. Current safety nets may not be enough to cover households from the loss of income, given the relatively poor targeting of the social assistance and social insurance programs.

However, once the current crisis abates, it is expected that the recent trend of falling poverty rates will continue.

## Project Spotlight

### Croatia Justice for Business Project



On March 31, 2020, the World Bank Board of Executive Directors approved a loan to Croatia for the Justice for Business Project in the amount of €100 million aimed at improving business regulatory procedures and judicial service standards for businesses and citizens.

The project will support the implementation of reforms

to improve the country's business environment and judicial sector services under the leadership of the Ministry of Justice, in coordination with the Ministry of Economy, Entrepreneurship and Crafts and the Ministry of Construction and Physical Planning.

A first set of activities will focus on reducing the administrative burden for companies in their interactions with the government by removing regulatory barriers to entering the market, simplifying the process of obtaining construction permits, and improving market functioning in the construction sector.

The project will also improve judicial services. For example, the use of electronic functions will be expanded to speed up response times and integrate case management systems across different courts.

The Zagreb, Vinkovci, Kutina, and Varazdin courthouses will be rehabilitated and upgraded for better court performance and user experience, and these transformational investments will help develop standard investment designs to be replicated across the country.

Improved infrastructure and services in the judicial sector will benefit both citizens and businesses.

Businesses will benefit from having a simpler and more transparent way to interact with government agencies and faster and more responsive judicial procedures, and all citizens will benefit from the more effective, efficient, and reliable administration of justice and the rule of law.

The "Country Snapshot" is a bi-annual update, highlighting the country's recent developments, economic outlook and major overview of the World Bank's partnership with the country. You can find the latest updates at <http://www.worldbank.org/croatia>



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