

CROATIA

Table 1 **2021**

Population, million	3.9
GDP, current US\$ billion	64.6
GDP per capita, current US\$	16619.4
International poverty rate (\$1.9) ^a	0.3
Lower middle-income poverty rate (\$3.2) ^a	0.6
Upper middle-income poverty rate (\$5.5) ^a	1.8
Gini index ^a	29.0
School enrollment, primary (% gross) ^b	93.2
Life expectancy at birth, years ^b	78.4
Total GHG Emissions (mtCO2e)	16.4

Source: WDI, Macro Poverty Outlook, and official data.
a/ Most recent value (2019), 2011 PPPs.
b/ Most recent WDI value (2019).

After a pronounced economic contraction in 2020, the Croatian economy strongly rebounded in 2021, posting a double-digit growth rate. In addition to domestic demand, economic activity was underpinned by a sharp revival of tourism and sizable exports of goods. Poverty is estimated to have declined to 1.6 percent in 2021. Over the medium term, growth is expected to moderate but remain relatively strong. However, downside risks to growth remain significant.

Key conditions and challenges

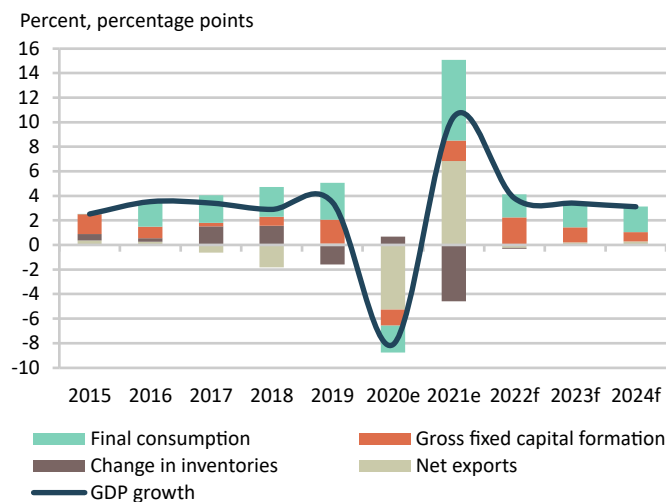
Croatia's economic recovery in 2021 was unexpectedly strong and output reached its pre-crisis levels by mid-2021, largely due to the reopening of the economy and fiscal and monetary support schemes. Furthermore, the relatively favorable epidemiological situation during summer months and the country's proximity to its main tourism originating markets resulted in a significant increase in tourist arrivals. Also, Croatia was relatively less affected by global supply chain bottlenecks given its export structure. Together with the strong global recovery, this led to a marked rise in exports of goods. However, underlying long-term growth remains relatively low. Results from the recent census suggest a decline in the total population. This means stronger potential long-term growth will hinge upon increase in productivity requiring improvements in business environment, public administration, education system and judiciary. While growth is set to remain relatively strong over the medium term, uncertainties related to inflation developments and the Russian invasion of Ukraine represent a significant risk for economic activity and public finances in the near-term. In early 2022, the government adopted a mitigation package worth around 1 percent of GDP for easing rising prices but the war in Ukraine might put additional pressure on inflation with associated risks of depleting

the real purchasing power of households, especially the poor and vulnerable. Furthermore, although the country's direct trade and financial linkages with Russia are limited, there could be significant indirect trade and investment effects via other EU countries. In addition, while the number of new COVID-19 cases has recently started to decline, relatively low vaccination rate and the potential emergence of new virus variants might impede recovery. Over the medium term, EU structural and investment funds as well as the new EU initiatives represent an opportunity for Croatia to accelerate the income convergence with the rest of the EU.

Recent developments

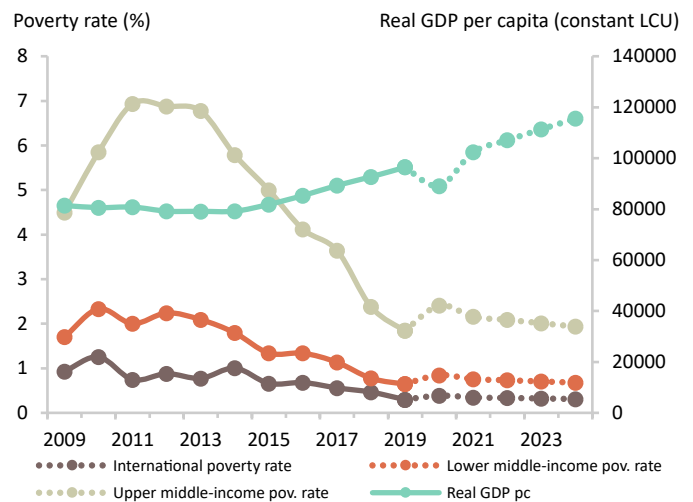
Following a contraction of 8.1 percent in 2020, real GDP in Croatia increased by 10.4 percent in 2021. Private consumption and investment activity provided strong support to overall growth, underpinned by an increase in consumer and business confidence, favorable financing conditions and inflow of EU funds. However, domestic demand lost some steam in the last quarter, which can be partly linked to the worsening of the epidemiological situation and buildup of inflation pressures. Contribution of net exports in 2021 was positive due to a sharp, albeit still partial, recovery of tourism and increase in exports of goods by one fifth compared to 2020. On the supply side, growth was also broad based with the services sector contributing the most to the rise in real gross value added.

FIGURE 1 Croatia / Real GDP growth and contributions to real GDP growth



Sources: CROSTAT, World Bank.

FIGURE 2 Croatia / Actual and projected poverty rates and real GDP per capita



Source: World Bank. Notes: see Table 2.

Favorable economic trends were followed by an increase in employment and wages, and in some sectors, notably construction, worker shortages became more pronounced and were mitigated by foreign labor. Inflation gradually intensified towards the end of the year, fueled by food and energy prices, and it continued to increase in 2022, reaching 6.3 percent in February. The general government deficit is estimated to have more than halved, to around 3.5 percent of GDP and public debt at the end of November 2021 stood at 80 percent of GDP, declining by 7.3 percentage points compared to the end of 2020.

The strong economic and employment rebound raised labor income. However, spikes in food prices in recent months put a burden on the most poor and vulnerable as they spend nearly 50 percent of their budget on necessities. Poverty, measured as the share of Croatian population living on less than \$5.5 a day at 2011 revised PPP prices, is estimated to have declined to 1.6 percent in 2021.

Outlook

Growth is set to moderate over the medium-term but will remain above the pre-pandemic trend. While global uncertainty related to the war in Ukraine is high, the Croatian economy could grow on average, by 3.5 percent, a year, over 2022-2024. However, there are significant downside risks related to the pandemic and the war in Ukraine. Investment activity underpinned by the inflow of EU funds is expected to pick-up strongly in 2022 and moderate thereafter. However, this primarily depends upon the implementation of government investment plans. Exports of goods and services are projected to support growth, but the pace of growth is expected to ease as tourism returns to pre-crisis levels and foreign demand moderates. Personal consumption growth might remain around 2.5 percent amid rising employment and wages. However, positive effects of the increase in wages on personal

consumption will be partly offset by higher inflation. Overall, inflation in 2023 and 2024 is projected to slow down due to the easing of global supply bottlenecks and tightened financial conditions. However, commodity price levels will remain elevated. General government deficit is likely to fall below 3 percent of GDP as of 2023. Also, public debt to GDP ratio is expected to continue declining, reaching 73.9 percent of GDP at the end of 2024.

Intensifying conflicts in the region is putting additional pressure on food and energy prices which were already on the rise. While the government has promptly introduced mitigation measures to cap gas price increases, it is still expected to rise on average by 20 percent. Moreover, regional political uncertainty and global supply disruptions can have implications for the economies of host countries of Croatian migrants. This can potentially have adverse impacts on remittances and income of Croatians at home. Nevertheless, poverty is expected to fall to 1.3 percent by 2024.

TABLE 2 Croatia / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2019	2020	2021e	2022f	2023f	2024f
Real GDP growth, at constant market prices	3.5	-8.1	10.4	3.8	3.4	3.1
Private Consumption	4.1	-5.3	10.0	2.2	2.5	2.7
Government Consumption	3.3	4.1	3.0	2.6	2.5	2.4
Gross Fixed Capital Investment	9.8	-6.1	7.6	10.5	5.3	3.2
Exports, Goods and Services	6.8	-22.7	33.3	6.6	5.3	5.1
Imports, Goods and Services	6.5	-12.3	14.7	6.9	4.7	4.4
Real GDP growth, at constant factor prices	3.6	-6.3	8.9	3.8	3.4	3.1
Agriculture	1.8	3.6	5.5	3.6	3.6	3.6
Industry	4.8	-1.6	6.7	4.0	3.0	3.0
Services	3.3	-8.4	9.9	3.7	3.5	3.1
Inflation (Consumer Price Index)	0.8	0.2	2.6	6.1	2.2	1.9
Current Account Balance (% of GDP)	3.0	-0.1	3.7	2.0	2.4	2.6
Net Foreign Direct Investment (% of GDP)	6.1	1.3	2.5	2.5	2.4	2.4
Fiscal Balance (% of GDP)	0.3	-7.4	-3.6	-3.2	-2.9	-2.6
Debt (% of GDP)	71.1	87.3	80.7	78.3	76.0	74.0
Primary Balance (% of GDP)	2.5	-5.4	-2.0	-1.7	-1.5	-1.4
International poverty rate (\$1.9 in 2011 PPP)^{a,b}	0.3	0.4	0.3	0.3	0.3	0.3
Lower middle-income poverty rate (\$3.2 in 2011 PPP)^{a,b}	0.6	0.7	0.6	0.6	0.5	0.5
Upper middle-income poverty rate (\$5.5 in 2011 PPP)^{a,b}	1.8	2.4	1.6	1.5	1.5	1.3
GHG emissions growth (mtCO₂e)	-1.1	-12.8	4.3	1.7	0.6	1.3
Energy related GHG emissions (% of total)	86.8	85.1	84.7	84.2	83.5	82.8

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.

a/ Calculations based on ECAPOV harmonization, using 2019-EU-SILC. Actual data: 2019. Nowcast: 2020-2021. Forecasts are from 2022 to 2024.

b/ Projection using neutral distribution (2019) with pass-through = 0.87 based on GDP per capita in constant LCU.