



Brussels, 21.11.2023
C(2023) 9510 final

COMMISSION OPINION

of 21.11.2023

on the Draft Budgetary Plan of Croatia

{SWD(2023) 951 final}

(Only the Croatian text is authentic)

COMMISSION OPINION

of 21.11.2023

on the Draft Budgetary Plan of Croatia

(Only the Croatian text is authentic)

GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013¹ lays down provisions for enhanced monitoring of budgetary policies in the euro area, in order to ensure that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact and the European Semester for economic policy coordination.
2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan, by 15 October, setting out the budgetary targets for the forthcoming year, and outlining the main aspects underlying the budgetary outlook for general government and its subsectors.
3. On 8 March 2023, the Commission adopted a Communication² providing fiscal policy guidance for 2024, which confirmed that the general escape clause of the Stability and Growth Pact will be deactivated at the end of 2023.
4. On 26 April 2023, the Commission presented three legislative proposals³ to implement a comprehensive reform of the EU fiscal framework. The central objective of the proposals is to strengthen public debt sustainability and to promote sustainable and inclusive growth through reforms and investments. In its proposals, the Commission aims at improving national ownership, simplifying the framework and moving towards a greater medium-term focus, combined with effective and more coherent enforcement. According to the Council Conclusions adopted on 14 March 2023⁴ and on 27 October 2023⁵, the objective is to conclude the legislative work in 2023. As a new legal framework, based on the outcome of the ongoing economic governance review, is not yet in place, the current legal framework continues to apply. The fiscal component of the Spring 2023 country-specific recommendations included elements of the legislative proposals of 26 April 2023 that were consistent with the existing legislation.

¹ Regulation (EU) No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, (OJ L 140, 27.5.2013, pp. 11).

² Communication from the Commission to the Council, 'Fiscal policy guidance for 2024', 8.3.2023, COM(2023) 141 final.

³ Commission Proposal for a Regulation of the European Parliament and of the Council on the effective coordination of economic policies and multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97, 26.4.2023, COM(2023) 240 final; Commission Proposal for a Council Regulation amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, 26.4.2023, COM(2023) 241 final; Commission Proposal for a Council Directive amending Directive 2011/85/EU on requirements for budgetary frameworks of the Member States, 26.4.2023, COM(2023) 242 final.

⁴ Council Conclusions on 'Orientations for a reform of the EU economic governance framework' of the ECOFIN Council meeting, 14.3.2023, 6995/1/23 – REV 1.

⁵ European Council meeting (26 and 27 October 2023) – Conclusions, EUCO 14/23.

5. As announced in its fiscal policy guidance⁶, the Commission will propose to the Council to open deficit-based excessive deficit procedures in spring 2024 on the basis of the outturn data for 2023, in line with the existing legal provisions. Member States were invited to take this into account when executing their 2023 budgets and preparing their Draft Budgetary Plans for 2024.
6. The Recovery and Resilience Facility⁷ provides financial support for the implementation of reforms and investments, notably to promote the green and digital transitions. The Facility also aims at increasing the resilience of the Union's energy system by reducing dependence on fossil fuels and diversifying energy supply at Union level ('REPowerEU objectives')⁸. The Facility will strengthen the resilience and potential growth of Member States' economies, which contributes to job creation and sustainable public finances. Part of this support takes the form of non-repayable financial support ("grants"), entailing a fiscal impulse financed by the Union. Together with cohesion policy funds and the Just Transition Mechanism, the Facility is supporting a fair and inclusive recovery in the EU, in line with the European Pillar of Social Rights.
7. Economic policy should continue to tackle the risks linked to high inflation and address long-term challenges. Despite declining, inflation in the euro area remains a concern. It is essential that inflation continues to fall and that inflation expectations remain well anchored, with consistent monetary and fiscal policies, while remaining agile in the face of high uncertainty. In particular, emergency energy support measures taken to respond to the energy price shock should be wound down, using the related savings to reduce the government deficits, as soon as possible in 2023 and 2024. Should renewed energy price increases necessitate new or continued support measures, these should be targeted at protecting vulnerable households and firms, as well as be fiscally affordable and preserve incentives for energy savings. Furthermore, Member States should continue to preserve nationally financed public investment and ensure the effective absorption of grants under the Recovery and Resilience Facility and of other EU funds, in particular to foster the green and digital transitions.

CONSIDERATIONS CONCERNING CROATIA

8. On 27 October 2023, Croatia submitted its Draft Budgetary Plan for 2024. On that basis and taking into account the Council Recommendation to Croatia of 14 July 2023⁹, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013. The Commission sent a letter to Croatia on 27 October 2023 with its preliminary observations on the Draft Budgetary Plan and asking for further information. Croatia replied to the Commission's letter on 3

⁶ Communication from the Commission to the Council, 'Fiscal policy guidance for 2024', 8.3.2023, COM(2023) 141 final.

⁷ Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility, (OJ L 57, 18.2.2021, p. 17).

⁸ Regulation (EU) 2023/435 of the European Parliament and of the Council of 27 February 2023 amending Regulation (EU) 2021/241 as regards REPowerEU chapters in recovery and resilience plans and amending Regulations (EU) No 1303/2013, (EU) 2021/1060 and (EU) 2021/1755, and Directive 2003/87/EC (OJ L 63, 28.2.2023, p. 1).

⁹ Council Recommendation on the 2023 National Reform Programme of Croatia and delivering a Council opinion on the 2023 Stability Programme of Croatia, OJ C 312, 1.9.2023, p. [97-104].

November 2023¹⁰. This information has been taken into account in the Commission's assessment of budgetary developments and risks.

9. According to the Draft Budgetary Plan, Croatia's real GDP is projected to grow by 2.8% in 2023 and 2024, while HICP inflation is forecast at 3.1% in 2024 (8.0% in 2023). In turn, according to the Commission 2023 autumn forecast, Croatia's real GDP is projected to grow by 2.5% in 2024 (2.6% in 2023), while HICP inflation is forecast at 2.4% in 2024 (8.1% in 2023). The difference between the HICP inflation projections for 2024 is mostly due to a stronger disinflationary effect of declining energy prices in the Commission forecast. Overall, the macroeconomic scenario underpinning the budgetary projections in the Draft Budgetary Plan appears to be in line with the Commission's 2023 autumn forecast for 2023 and 2024. Croatia complies with the requirement of Article 4(4) of Regulation (EU) No 473/2013, since the Draft Budgetary Plan is based on independently endorsed macroeconomic forecasts.
10. According to the Draft Budgetary Plan, Croatia's general government deficit is projected to increase to 1.9% of GDP in 2024 (from 0.3% in 2023). This increase is mainly driven by strong growth in expenditure with public wages and social benefits increased in response to high inflation, measures to contain the impact of inflation on real incomes, a reform of the wage-setting framework, as well as discretionary tax measures and higher nationally-funded investment. The general government debt-to-GDP ratio is set to decrease to 58.0% at the end of 2024 (60.7% at the end of 2023). In turn, according to the Commission 2023 autumn forecast, Croatia's general government deficit is projected to increase to 1.8% of GDP in 2024 (from 0.1% in 2023), while the general government debt-to-GDP ratio is set to decrease to 58.8% at the end of 2024 (from 60.8% at the end of 2023).
11. Based on the Commission's estimates, the fiscal stance¹¹ is projected to be expansionary at 1.2% of GDP in 2024, following an expansionary fiscal stance of 0.9% in 2023.
12. The Draft Budgetary Plan assumes that expenditure amounting to 1.6% of GDP will be financed by non-repayable support ("grants") from the Recovery and Resilience Facility in 2024, compared to 0.9% of GDP in 2023. This is in line with the assumptions underlying the Commission 2023 autumn forecast. Expenditure financed by Recovery and Resilience Facility grants will enable high-quality investment and productivity-enhancing reforms without a direct impact on the general government balance and debt of Croatia. The Draft Budgetary Plan also assumes expenditure backed by loans from the Recovery and Resilience Facility, amounting to 0.8% of GDP in 2024, compared with 0.0% of GDP in 2023.
13. According to the Commission 2023 autumn forecast, taking into account the information contained in the Draft Budgetary Plan, the measures adopted to mitigate the economic and social impact of the increase in energy prices are expected to remain in place until the end of the first quarter of 2024. They consist of measures

¹⁰ The Commission's letter and the reply by Croatia have been published: https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/stability-and-growth-pact/annual-draft-budgetary-plans-dbps-euro-area-countries/draft-budgetary-plans-2024_en

¹¹ The fiscal stance is measured as the change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures, excluding one-off and cyclical unemployment expenditure, but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to medium-term (10-year) average potential GDP growth rate, expressed as a ratio to nominal GDP.

already in place until end of March 2024, and extended measures that were in place only until October 2023 (in particular extended measures are related to price caps for electricity and targeted social assistance to pensioners and other vulnerable groups). There is a 0.1% of GDP difference between the Commission and DBP assumption regarding energy measures in 2024-2025, as the Commission assumes that the Croatia Energy Company (HEP) will not pay any dividends to the general government, due to losses related to the energy price cap measures. In addition, the Draft Budgetary Plan includes several new revenue measures for 2024 that are not directly related to energy price developments. These include a broadening of the scope for tax exemptions for personal income taxes and pension contributions that negatively affect revenue and an increase in the tax rate for capital and property income that positively impacts revenue. The aggregate revenue impact of these measures is estimated by the Commission at -0.4% of GDP in 2024 and are expected to have a permanent effect on public finances.

14. On 14 July 2023, the Council recommended that Croatia ensure a prudent fiscal policy, in particular by limiting the nominal increase in nationally financed net primary expenditure¹² in 2024 to not more than 5.1%. According to the Commission 2023 autumn forecast, Croatia's net nationally financed primary expenditure is projected to increase by 10.4% in 2024, which is above the recommended maximum growth rate. This excess spending over the recommended maximum growth rate in net nationally financed primary expenditure corresponds to 2.1% of GDP in 2024. This risks being not in line with what was recommended by the Council.
15. Moreover, the Council recommended that Croatia take action to wind down the emergency energy support measures in force, using the related savings to reduce the government deficit, as soon as possible in 2023 and 2024. The Council further specified that, should renewed energy price increases necessitate new or continued support measures, Croatia should ensure that these were targeted at protecting vulnerable households and firms, fiscally affordable, and preserve incentives for energy savings. According to the Commission 2023 autumn forecast, the net budgetary cost¹³ of energy support measures is projected at 1.8% of GDP in 2023, 0.5% in 2024 and 0.1% in 2025. In particular, the electricity and gas price caps measures are legislated to remain in force until the end of March 2024. If the related savings were used to reduce the government deficit, as recommended by the Council, these projections would imply a fiscal adjustment of 1.3% of GDP in 2024, whereas net nationally financed primary expenditure¹⁴ provides an expansionary contribution to the fiscal stance of 1.5% of GDP in that year. The energy support measures are not projected to be wound down as soon as possible in 2023 and 2024, as the size of the measures remains relatively high in the first quarter of 2024. This risks being not in line with what was recommended by the Council. Moreover, the related savings are not projected to be fully used to reduce the government deficit. This risks being not in line with the Council recommendation. The net budgetary cost of energy support

¹² Net primary expenditure is defined as nationally financed expenditure net of discretionary revenue measures and excluding interest expenditure as well as cyclical unemployment expenditure.

¹³ The figure represents the level of the annual budgetary cost of those measures, including revenue and expenditure and, where applicable, net of the revenue from taxes on windfall profits of energy suppliers.

¹⁴ This contribution is measured as the change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures, excluding one-off and cyclical unemployment expenditure, as well as expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to the medium-term (10-year) average potential nominal GDP growth rate, expressed as a ratio to nominal GDP.

measures targeted at protecting vulnerable households and firms is estimated at 0.0% of GDP in 2024 (0.3% in 2023), of which 0.0% of GDP preserve the price signal to reduce energy demand and increase energy efficiency (0.1% in 2023).

16. In addition, the Council recommended that Croatia preserve nationally financed public investment and ensure the effective absorption of Recovery and Resilience Facility grants and other EU funds, in particular to foster the green and digital transitions. According to the Commission 2023 autumn forecast, nationally financed public investment is projected to increase to 3.2% of GDP in 2024 (from 2.7% of GDP in 2023) and, therefore, it is expected to be preserved. This is in line with what was recommended by the Council. In turn, public expenditure financed from revenues from EU funds, including Recovery and Resilience Facility grants, is expected to decrease to 2.7% of GDP in 2024 (from 3.0% of GDP in 2023). This decrease is driven by the end of the 2014-2020 programming period of EU structural funds, for which funds are available until 2023.
17. Furthermore, on 14 July 2023, the Council also recommended that, for the period beyond 2024, Croatia continue to pursue a medium-term fiscal strategy of gradual and sustainable consolidation, combined with investments and reforms conducive to higher sustainable growth, to achieve a prudent medium-term fiscal position. The Draft Budgetary Plan does not include budgetary projections beyond 2024.
18. According to the Commission's forecast, the growth of net nationally financed primary expenditure is projected to not respect the recommended maximum growth rate in 2024.

Moreover, according to the Commission 2023 autumn forecast, and taking into consideration the information included in Croatia's Draft Budgetary Plan, the emergency energy support measures are not expected to be wound down as soon as possible in 2023 and 2024. Furthermore, the related savings are not projected to be fully used to reduce the general government deficit in 2024.

However, Croatia is expected to preserve nationally financed public investment. Croatia should also continue to ensure the effective absorption of Recovery and Resilience Facility grants and other EU funds.

Overall, the Commission is of the opinion that the updated Draft Budgetary Plan of Croatia risks being not in line with the Council Recommendation of 14 July 2023. Therefore, the Commission invites Croatia to take the necessary measures within the national budgetary process to ensure that fiscal policy in 2024 will be in line with the Council Recommendation of 14 July 2023.

However, the Commission projects Croatia's headline budget deficit is projected at 1.8% of GDP in 2024, below the Treaty reference value of 3% of GDP, and the government debt ratio at 58.8% in 2024, going below the Treaty reference value of 60% of GDP, and 19.3 percentage points of GDP below the ratio at end 2021.

A comprehensive description of progress made with the implementation of the Council's country-specific recommendations will be included in the 2024 Country Report and assessed in the context of the Council's country-specific recommendations to be recommended by the Commission in spring 2024.

Table: Key macroeconomic and fiscal figures

	2022	2023		2024	
	Outturn	DBP	COM	DBP	COM
Real GDP (% change)	6.3	2.8	2.6	2.8	2.5
HICP inflation (%; annual average)	10.7	8.0	8.1	3.1	2.4
General government balance (% of GDP)	0.1	-0.3	-0.1	-1.9	-1.8
Primary balance (% of GDP)	1.5	1.2	1.0	-0.5	-0.7
General government gross debt (% of GDP; at end-year)	68.2	60.7	60.8	58.0	58.8
	COM	COM		COM	
Fiscal stance (*) (% of GDP)	0.3	-0.9		-1.2	
Fiscal adjustment (**) (% of GDP)	0.2	-0.5		-1.5	
Change in total net budgetary cost of energy support measures (***) (% of GDP)	1.5	0.2		-1.3	
Growth in net nationally financed primary expenditure (% change) (A)				10.4	
Recommended maximum growth rate of net nationally financed primary expenditure (****) (% change) (B)				5.1	
Difference from recommended growth in net nationally financed primary expenditure (pps.) (B-A)				-5.3	
[If net expenditure grows above CSR] Impact on fiscal adjustment of deviation in net nationally financed primary expenditure compared with the Council recommendation (*****) (% of GDP)				2.1	

Notes:

(*) Change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures (and COVID-19 pandemic-related temporary emergency measures), excluding one-off and cyclical unemployment expenditure, but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to the medium-term (10-year) average potential nominal GDP growth rate. A negative (positive) sign indicates an excess (a shortfall) of net primary expenditure growth over medium-term potential GDP growth, corresponding to an expansionary (a contractionary) fiscal stance.

(**) Change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures (and COVID-19 pandemic-related temporary emergency measures), excluding one-off and cyclical unemployment expenditure, as well as expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to the medium-term (10-year) average potential nominal GDP growth rate. A negative (positive) sign indicates an excess (a shortfall) of net nationally financed primary expenditure growth over medium-term potential GDP growth, corresponding to an expansionary (a contractionary) fiscal adjustment.

(***) Energy support measures less revenue from new taxes and levies on windfall profits by energy producers.

(****) According to the Council Recommendation 'on the 2023 National Reform Programme of Croatia and delivering a Council opinion on the 2023 Stability Programme of Croatia', (OJ C 312, 1.9.2023, p. 97).

(*****). Excess in growth of net nationally financed primary expenditure over the recommended maximum growth rate, expressed as a percentage of GDP.

'DBP' 2024 Draft Budgetary Plan, 'COM' Commission 2023 autumn forecast.

Done at Brussels, 21.11.2023

For the Commission
Paolo GENTILONI
Member of the Commission