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**Assessment of the 2015 Convergence Programme for  
CROATIA**

*(Note prepared by DG ECFIN staff)*

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## **1. INTRODUCTION**

This document assesses Croatia's April 2015 Convergence Programme (hereafter called Convergence Programme), which was submitted to the Commission on 30 April 2015 and covers the period 2014-2018. It was approved by the government in its session of 30 April 2015. The Convergence Programme was neither presented nor discussed in the national parliament.

Croatia is currently subject to the corrective arm of the Stability and Growth Pact. The Council opened the Excessive Deficit Procedure based on both deficit and debt on 28 January 2014. Croatia was recommended to correct the excessive deficit situation by 2016. The year following the correction of the excessive deficit, Croatia will be subject to the preventive arm of the Pact and should ensure sufficient progress towards its MTO. As the debt-to-GDP ratio in 2016 is projected at 93.9%, exceeding the 60% of GDP reference value, Croatia will also be subject to the debt reduction benchmark.

This document complements the Country Report published on 26 February 2015 and updates it with the information included in the Convergence programme. Section 2 presents the macroeconomic outlook underlying the Convergence Programme and assesses it based on the Commission 2015 spring forecast. The following section presents the recent and planned budgetary developments, according to the Convergence Programme. In particular, it includes an overview on the medium term budgetary plans, an assessment of the measures underpinning the Stability Programme and a risk analysis of the budgetary plans based on Commission forecast. Section 4 assesses compliance with the rules of the Stability and Growth Pact, including on the basis of the Commission forecast. Section 5 provides an overview of long-term sustainability risks and Section 6 of recent developments and plans regarding the fiscal framework and the quality of public finances. Section 7 draws the main conclusions.

## **2. MACROECONOMIC OUTLOOK**

In 2014, the Croatian economy contracted for the sixth consecutive year. At -0.4%, the rate of GDP contraction nevertheless abated compared to the previous year. The external sector performed remarkably well, with exports of goods and services progressing by 6.3% (see Table 1). The contraction of internal demand was however particularly strong, especially due to a further sharp fall in investment activity.

The macroeconomic scenario in the Convergence Programme indicates that Croatia is set to return to positive growth in 2015. Real GDP is projected to grow by a modest 0.4% y-o-y. Internal demand is expected to continue to contract, but at a declining pace, as private consumption improves by 0.5% y-o-y and the fall of investment activity decelerates to -1.3% y-o-y. The external sector is set to continue to be the main driver of growth, with an expected strong performance of exports of goods and services leading to a contribution of net exports to growth of 0.5 pp. In 2016, the restraint of government consumption is expected to continue, but internal demand is forecast to finally contribute positively to GDP, on the back of a long heralded rebound in investments, also thanks to additional measures to increase absorption of the EU structural and investment funds, and a further expansion of private consumption. Combined with the continuing positive contribution of external demand, GDP growth is set to

attain 1% in 2016. Employment is expected to broadly stagnate in 2015 and 2016. The growth of compensation of employees per head and GDP deflator appear broadly realistic.<sup>1</sup>

**Table 1: Comparison of macroeconomic developments and forecasts**

	2014		2015		2016		2017	2018
	COM	CP	COM	CP	COM	CP	CP	CP
Real GDP (% change)	-0.4	-0.4	0.3	0.4	1.2	1.0	1.2	1.5
Private consumption (% change)	-0.7	-0.7	0.1	0.5	0.5	0.3	0.5	1.1
Government consumption (% change)	-1.9	-1.9	0.0	-1.2	0.9	-1.4	-1.0	-0.6
Gross fixed capital formation (% change)	-4.0	-4.0	-1.8	-1.3	1.6	1.8	3.2	3.6
Exports of goods and services (% change)	6.3	6.3	3.7	3.7	4.6	4.6	4.8	4.8
Imports of goods and services (% change)	3.0	3.0	2.4	2.8	4.0	4.0	4.5	5.0
<i>Contributions to real GDP growth:</i>								
- Final domestic demand	-1.6	-1.6	-0.3	-0.2	0.8	0.3	0.7	1.2
- Change in inventories	-0.2	-0.2	0.0	0.0	0.0	0.2	0.2	0.1
- Net exports	1.4	1.4	0.7	0.5	0.4	0.4	0.3	0.1
Output gap <sup>1</sup>	-3.5	-3.5	-3.2	-3.0	-2.1	-2.1	-1.1	0.0
Employment (% change) <sup>2</sup>	-0.7	-0.7	0.0	-0.2	0.5	0.1	0.8	1.3
Unemployment rate (%)	17.3	17.3	17.0	17.1	16.6	16.8	15.9	14.3
Labour productivity (% change) <sup>2</sup>	0.4	0.3	0.1	0.5	0.6	0.8	0.4	0.2
HICP inflation (%)	0.2	n.a.	0.1	n.a.	1.3	n.a.	n.a.	n.a.
GDP deflator (% change)	0.0	0.0	0.0	0.2	1.2	0.8	1.1	1.4
Comp. of employees (per head, % change) <sup>2</sup>	1.6	1.1	1.3	0.7	1.5	0.8	1.4	1.7
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	0.6	0.8	1.8	1.9	2.8	2.7	2.9	3.0
<b>Note:</b>								
<sup>1</sup> In percent of potential GDP, with potential GDP growth recalculated by the Commission on the basis of the programme scenario, using the commonly agreed methodology.								
<sup>2</sup> COM figures have been adjusted to correct for breaks in the historical series.								
<b>Source:</b>								
Commission 2015 spring forecast (COM); Convergence Programme (CP).								

According to the Programme, 2017 and 2018 should witness an acceleration of real GDP growth to 1.2% and 1.5%, respectively. The acceleration of investment is expected to add to the moderate expansion of private consumption. Thus, despite continued restraint of government consumption, the contribution to growth of internal demand will accelerate to 0.7 pp. and 1.2 pps, respectively, on the back of the recovery of private consumption and sustained investment activity. The performance of exports is set to remain positive over the whole horizon of the Convergence Programme, with the sustained growth of exports in 2017 and 2018 implying a steady improvement in Croatia's external competitiveness. However, as the acceleration of internal demand – and especially investment – will drive up imports, the net contribution of external demand is set to gradually decrease from 0.4 pp. in 2016 to 0.3

<sup>1</sup> The dynamics of employment, compensation per employees (per head) and productivity in the Commission spring forecast were affected by breaks in the series. Figures have been adjusted to correct for these breaks and provide a comparable basis for the assessment of the Convergence Programme.

and 0.1 pp. in 2017 and 2018, respectively. The pick-up of growth in 2017 and 2018 is set to bring about an increase in employment, and the unemployment rate is projected to decrease progressively to 14.3% in 2018. The output gap as recalculated by the Commission based on the information in the programme, following the commonly agreed methodology, is set to close in 2018, from a gap of -3.0% in 2015 (for 2014-2016, broadly similar to the projections in the Commission 2015 spring forecast).

In the light of the Commission 2015 spring forecast, the macroeconomic scenario seems somewhat favourable in the first two years of the programme. Whereas headline growth figures are broadly comparable for 2015, the forecast by the authorities factors in a stronger recovery of private consumption, despite a more negative view on employment growth and compensation per employee, but also a stronger restraint of government expenditure, which, if it materialises, is likely to negatively affect the growth outlook. The 2016 outlook seems slightly more realistic— as indeed the contribution of internal demand is only 0.3 pp. as opposed to the European Commission's 0.8 pp. (which reflects the customary no policy change assumption leading to a moderate pick-up in government consumption). The weaker contribution of internal demand also reflects a weaker growth of employment and compensation per employee. Despite lower contribution of internal demand, the positive contribution of inventories in 2016 pushes up the real GDP growth rate closer to the Commission forecast. In the outer years, the pace of contraction in government consumption is set to abate, so the composition of internal demand appears broadly plausible. The somewhat lower employment growth in the Programme appears consistent with the dynamics of internal demand, while the recovery of both employment and compensation of employees in 2017 and 2018 is in line with output growth. By contrast, the external outlook appears optimistic. Overall, the macroeconomic scenario underpinning the Convergence Programme seems somewhat favourable.

### **3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS**

#### **3.1. Deficit developments in 2014**

In 2014, the general government deficit reached 5.7% of GDP, significantly above the target of last year's Convergence Programme, which planned a deficit of 4.4% of GDP. The difference of 1.3% of GDP between the planned and actual deficit can be explained by (1) statistical revisions affecting the previous years' deficit<sup>2</sup>, accounting for almost 0.5 pp. of the difference; (2) significantly lower-than-anticipated expenditure developments (reducing the deficit outcome by 2.1 pps. compared to plans), which were however more than offset by (3) significantly lower-than-anticipated revenue growth (increasing the deficit outcome by 2.9 pps. compared to plans). In turn, the revenue shortfall in 2014 can be explained in part by a statistical reclassification of (one-off) revenue from the transfer of pension fund assets from the second to the first pillar (0.8 pp., which under ESA95, counted as an incoming capital transfer, but under the current ESA 2010 is no longer affecting the deficit). Most of the remaining part reflects revenue developments considerably below what could be expected based on the development of the tax basis and normal elasticities, which more than offset revenue increasing discretionary measures (in particular the increase of social contributions due to the change of health contributions rate).

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<sup>2</sup> According to Eurostat analysis of revisions to government deficit and debt of EU Member States for 2010-2013, published after the switchover of fiscal statistics to a new standard, the revisions of the Croatian deficit stem mainly from reasons other than introduction of ESA 2010.

### **3.2. Target for 2015 and medium-term strategy**

#### **The target for 2015**

In 2015, the authorities aim for a general government deficit of 5.0% of GDP, a decrease from 5.7% of GDP in 2014, but well above the recommended target of 3.5% of GDP. The share of total revenue in GDP is projected to increase by 0.6 pp., while total expenditure is expected to remain broadly stable in 2015. The authorities aim to achieve this target on the basis of revenue increasing measures totalling 0.4% of GDP, and expenditure decreasing measures of 1.1% of GDP (see table below). However, the baseline scenario against which these figures are appraised is not specified. The fiscal consolidation efforts projected in the programme originate from the central government level, which is planned to reduce its deficit from 6.1% of GDP in 2014 to 5.0% in 2015. These efforts are partly offset by local authorities and social security, which are planned to return from a small surplus in 2015 (0.3 and 0.1% of GDP respectively) to a broadly balanced budget position.

In the 2014 Convergence Programme, the authorities were aiming for a deficit of 3.5% of GDP, 1.5% of GDP lower than the current target. The revised target for 2015 reflects almost entirely the impact of the different outcome of 2014, for the general government balance, as well as for the breakdown in revenue and expenditure, with the implicit projected growth rates for revenue and expenditure being nearly identical to the ones in the 2014 Convergence Programme.

In the Commission 2015 spring forecast, the general government deficit in 2015 is projected at 5.6% of GDP, an improvement of 0.1 pp. of GDP compared to the outcome in 2014. The difference between the Convergence Programme target for 2015 and the Commission 2015 spring forecast reflects slightly lower revenue projections (0.2 pp.) as well as a higher expenditure forecast (0.4 pp.), stemming to a large extent from a different assessment of the impact of planned consolidation measures. For several of these measures, mostly on the expenditure side, the impact estimated by the Commission is lower due to the implementation risks mirrored in the track record.

The improvement in the structural balance in 2015, as recalculated by the Commission on the basis of the information in the programme, following to the commonly agreed methodology, is projected at 0.4% of GDP. At the same time, in the Commission 2015 spring forecast the structural balance in 2015 deteriorates by 0.1% of GDP (a difference which can be entirely explained by the difference in the headline balance).

#### **The medium-term strategy**

The main aim of the Croatian fiscal policy in the medium term, as defined by the programme, is to correct the excessive deficit by 2017<sup>3</sup> and bring the headline deficit down to 2.4% of GDP by 2018. Roughly two thirds of the planned deficit reduction is located on the expenditure side, and one third on the revenue side.

In the medium term, the reduction of the general government deficit in the programme appears somewhat backloaded, with the biggest efforts (both in terms of headline and structural balance) concentrated in the 2016-17 period. The driving factor throughout the programme period is the central government deficit.

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<sup>3</sup> This is one year later than foreseen in the EDP recommendation. However, based on the findings of the Commission 2015 spring forecast, the bottom-up fiscal effort delivered by Croatia in 2014 is in line with what was recommended by the Council (see also Section 4 below).

The programme does not foresee a further structural consolidation effort in 2018. Moreover, the Convergence Programme does not contain a reference to the medium-term objective (MTO).<sup>4</sup>

**Table 2: Composition of the budgetary adjustment**

(% of GDP)	2014	2015		2016		2017	2018	Change: 2014-2018
	COM	COM	CP	COM	CP	CP	CP	CP
<b>Revenue</b>	<b>42.3</b>	<b>42.7</b>	<b>42.9</b>	<b>42.9</b>	<b>43.3</b>	<b>43.7</b>	<b>43.5</b>	<b>1.2</b>
<i>of which:</i>								
- Taxes on production and imports	18.7	18.7	18.9	18.8	19.1	19.2	19.2	0.5
- Current taxes on income, wealth, etc.	5.9	5.7	5.5	5.8	5.6	5.6	5.6	-0.3
- Social contributions	11.8	12.3	11.8	12.3	11.8	11.8	11.8	0.0
- Other (residual)	6.0	6.1	6.6	6.0	6.9	7.2	6.9	1.0
<b>Expenditure</b>	<b>48.0</b>	<b>48.3</b>	<b>47.9</b>	<b>48.6</b>	<b>47.3</b>	<b>46.4</b>	<b>45.9</b>	<b>-2.1</b>
<i>of which:</i>								
- Primary expenditure	44.5	44.6	44.3	44.9	43.5	42.6	42.1	-2.5
<i>of which:</i>								
Compensation of employees	11.7	11.7	11.5	11.5	11.3	11.0	10.8	-0.9
Intermediate consumption	8.0	8.2	7.9	8.4	7.6	7.4	7.2	-0.8
Social payments	16.5	16.9	16.5	17.0	16.3	16.1	16.1	-0.4
Subsidies	2.0	1.9	2.0	1.9	1.8	1.7	1.7	-0.4
Gross fixed capital formation	3.6	3.4	3.8	3.5	4.0	4.0	4.0	0.4
Other (residual)	2.6	2.6	2.6	2.5	2.4	2.3	2.3	-0.3
- Interest expenditure	3.5	3.7	3.6	3.7	3.8	3.9	3.9	0.4
<b>General government balance (GGB)</b>	<b>-5.7</b>	<b>-5.6</b>	<b>-5.0</b>	<b>-5.7</b>	<b>-3.9</b>	<b>-2.7</b>	<b>-2.4</b>	<b>3.3</b>
<b>Primary balance</b>	<b>-2.2</b>	<b>-1.9</b>	<b>-1.4</b>	<b>-2.0</b>	<b>-0.2</b>	<b>1.1</b>	<b>1.4</b>	<b>3.7</b>
One-off and other temporary	-0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.1
<b>GGB excl. one-offs</b>	<b>-5.7</b>	<b>-5.6</b>	<b>-5.0</b>	<b>-5.7</b>	<b>-3.9</b>	<b>-2.7</b>	<b>-2.4</b>	<b>3.2</b>
Output gap <sup>1</sup>	-3.5	-3.2	-3.0	-2.1	-2.1	-1.1	0.0	3.5
Cyclically-adjusted balance <sup>1</sup>	-4.1	-4.1	-3.6	-4.7	-3.0	-2.2	-2.4	1.7
<b>Structural balance (SB)<sup>2</sup></b>	<b>-4.0</b>	<b>-4.2</b>	<b>-3.6</b>	<b>-4.7</b>	<b>-3.0</b>	<b>-2.2</b>	<b>-2.4</b>	<b>1.6</b>
Structural primary balance <sup>2</sup>	-0.5	-0.5	0.0	-1.0	0.8	1.6	1.4	2.0
<b>Notes:</b>								
<sup>1</sup> Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by the Commission on the basis of the programme scenario, using the commonly agreed methodology.								
<sup>2</sup> Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.								
<b>Source:</b>								
Convergence Programme (CP); Commission 2015 spring forecast (COM); Commission calculations.								

The current programme targets differ significantly from the targets in the 2014 Convergence Programme, mostly on account of the substantially different starting position (see above).

<sup>4</sup> The Economic Policy Committee endorsed the long-term expenditure projections for the 2015 Ageing Report in February 2015. On that basis, the Commission is expected to set a minimum MTO for Croatia in September 2015, together with updates of minimum MTOs for other Member States.

Revised targets also need to be seen against a significantly less optimistic macroeconomic scenario in the current programme, as well as the change in policies, for example regarding the recurrent property taxation, which was envisaged to be introduced in 2016 in last year's Convergence Programme, but is no longer planned in the current programme.

The budgetary targets in the programme require significant additional consolidation measures, in particular for 2016 and 2017. At present, for 2016 and 2017 the programme only foresees the full year impact of measures introduced in the course of 2015. No additional measures have been specified. Accordingly, the Programme suggests that expenditure should gradually decline as a result of previously introduced measures, while the share of revenue in GDP remains broadly unchanged.

### Measures underpinning the programme

#### Main budgetary measures

Revenue	Expenditure
<b>2014</b>	
<ul style="list-style-type: none"> <li>• Increase of the rate of healthcare contributions from 13% to 15% (+0.49% of GDP)</li> <li>• Increased social security contributions due to the shift of part of the future pension contributions to first pillar (+0.12% of GDP)</li> <li>• Higher fuel excises (+0.11% of GDP)</li> <li>• Other revenues side measures: changes in the lottery and gambling taxes, SOEs dividend and profit withdrawal, increase of telecom fees and other concession fees (+0.1% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Lower intermediate consumption due to savings, among other, on maintenance costs, transportation costs, IT services (-0.3% of GDP)</li> <li>• Reduction of subsidies, mostly to shipyards, HBOR and railways (-0.4% of GDP)</li> <li>• Savings in social transfers, mostly in health sector and privileged pensions' outlays (-0.3% of GDP)</li> <li>• Reduction of current and capital transfers, mostly due to replacement with EU funding (-0.1% of GDP)</li> <li>• Lower public investment (-0.1% of GDP)</li> <li>• Extrabudgetary users and other general government entities, mainly in Croatian Roads and Croatian Waters (-0.4% of GDP)</li> </ul>
<b>2015</b>	
<ul style="list-style-type: none"> <li>• Increase of the rate of healthcare contributions from 13% to 15% (+0.25% of GDP); a residual effect of the measure introduced in 2014</li> <li>• Changes in the lottery and gambling taxes (+0.06% of GDP); a residual effect of the measure introduced in 2014</li> <li>• Increased social security contributions due to the shift of part of the future pension contributions to first pillar (+0.08% of GDP); a residual effect of the measure introduced in 2014</li> </ul>	<ul style="list-style-type: none"> <li>• Higher fuel and tobacco excises (+0.16% of GDP)</li> <li>• Lower intermediate consumption due to the reorganisation of court network, agencies network and external providers of various services; (-0.13% of GDP)</li> <li>• Reduction of subsidies for agriculture and HBOR and other, such as innovation guarantee fund, entrepreneurial support, housing saving subsidies, railway transport support (-0.18% of GDP)</li> </ul>



<b>Revenue</b>	<b>Expenditure</b>
<ul style="list-style-type: none"> <li>• Personal income tax rebate<sup>5</sup> (-0.54% of GDP)</li> <li>• Increase of revenue of the local government units as a reaction to their loss of income due to the introduction of personal income tax rebate (+0.1% of GDP)</li> <li>• Tax on savings interest (+0.09% of GDP)</li> <li>• SOEs dividend and profit withdrawal (+0.18% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Other central government cuts – compensation of employees, public investment in health sector, transfers (-0.16% of GDP)</li> <li>• Savings in extrabudgetary users, in particular Croatian Roads, Croatian Waters, Croatian Health Insurance Fund, Croatian Highways and Croatian Railways Infrastructure Operator (-0.4% of GDP)</li> <li>• Reduction of expenditure of the local government units as a reaction to their loss of income due to the introduction of personal income tax rebate (-0.2% of GDP)</li> </ul>
<b>2016</b>	
<ul style="list-style-type: none"> <li>• Higher fuel and tobacco excises (+0.06% of GDP); a residual effect of the measure introduced in 2014</li> <li>• New treatment of reinvested earnings' benefit in the corporate income tax system (+0.15% of GDP)</li> <li>• Harmonisation of local communal charges collection (+0.09% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Further reduction of subsidies in agriculture, regional development, culture and railways, mostly through substitution by EU funds (-0.21% of GDP)</li> <li>• Lower intermediate consumption due to further rationalisation of court network and centralized public procurement for postal services and electrical energy (-0.16% of GDP)</li> <li>• Reduction of social benefits and health sector expenditure (-0.16% of GDP)</li> <li>• Savings on the compensation of employees through the comprehensive reform of the public wage bill (-0.13% of GDP)</li> <li>• Savings in the system of agencies (-0.1% of GDP)</li> </ul>
<b>2017</b>	
<ul style="list-style-type: none"> <li>• No measures specified in the Convergence Programme</li> </ul>	<ul style="list-style-type: none"> <li>• No measures specified in the Convergence Programme</li> </ul>
<b>2018</b>	
<ul style="list-style-type: none"> <li>• No measures specified in the Convergence Programme</li> </ul>	<ul style="list-style-type: none"> <li>• No measures specified in the Convergence Programme</li> </ul>
<p><u>Note:</u> The budgetary impact in the table is the impact reported in the programme, i.e. by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure.</p>	

The consolidation measures as presented in the programme are subject to significant implementation risks. In particular, some of the expenditure reducing measures (such as cuts in expenditure of State-owned enterprises (SOEs) in the transportation sector) have been proven to be difficult to implement given the limited control of government over the spending plans of these enterprises. Also, similarly to the last year's Convergence Programme, the

<sup>5</sup> As from January 2015, the personal allowance was increased from HRK 2200 to 2600 per month and the lower limit for the highest marginal tax rate of 40% was increased from HRK 8800 to HRK 13200.

programme envisages a several small expenditure cuts dispersed across many different categories, items and also levels of government (including extra-budgetary users). These cuts are often not (yet) underpinned by well-designed policies to reduce expenditure needs and require further implementation measures by other budgetary users, casting doubt on their effectiveness and durable nature. Likewise, government plans to increase the withdrawal of the SOEs profits are also facing implementation risks (also taking into account that similar measures in the past have underperformed) while the impact is likely to be temporary. These elements to a large extent explain the difference between the Convergence Programme budgetary targets and the Commission forecast.

Furthermore, a number of the fiscal consolidation measures envisaged in the programme will directly or indirectly have an impact on investment (thus also affecting growth in the medium term). Several measures also seem to have only a temporary positive impact on the budget. Finally the Convergence Programme does not include any detailed plans to implement (or even publish) the findings of the recently completed expenditure review, which could be a very useful starting point for improving the efficiency of public spending.

### **3.3. Debt developments**

The debt-to-GDP ratio in Croatia has been on a rapidly increasing path and stood at 85% at the end of 2014 (see Table 3). Low economic growth in combination with large general government deficits were the main driving forces behind the rising general government debt ratio. Debt assumptions (also related to the restructuring of certain industries) as well as the reclassification of a number of highly-indebted companies into the general government sector (also in relation to the introduction of ESA2010) also contributed to the rising debt. In particular, the statistical reclassification of Croatian Motorways and Motorway Rijeka-Zagreb in autumn 2014 and of HBOR in spring 2015 increased the debt ratio by more than 13 pps. of GDP which also explains to a large extent the considerable difference between current debt projections and those in previous programmes (Figure 1).

Debt is projected to increase further during the programme period, on the back of a continued primary budget deficit and a sizeable interest rate growth differential. The programme foresees fiscal consolidation to stabilise the public debt at around 92.5% of GDP in 2017.

**Table 3: Debt developments**

(% of GDP)	Average 2011-2013	2014	2015		2016		2017	2018
			COM	CP	COM	CP	CP	CP
<b>Gross debt ratio<sup>1</sup></b>	<b>71.2</b>	<b>85.0</b>	<b>90.5</b>	<b>89.8</b>	<b>93.9</b>	<b>92.0</b>	<b>92.5</b>	<b>92.4</b>
Change in the ratio	7.9	4.4	5.5	4.8	3.5	2.2	0.5	-0.1
<i>Contributions<sup>2</sup> :</i>								
<b>1. Primary balance</b>	<b>2.8</b>	<b>2.2</b>	<b>1.9</b>	<b>1.4</b>	<b>2.0</b>	<b>0.2</b>	<b>-1.1</b>	<b>-1.4</b>
<b>2. “Snow-ball” effect</b>	<b>3.2</b>	<b>3.8</b>	<b>3.3</b>	<b>3.2</b>	<b>1.5</b>	<b>2.3</b>	<b>1.8</b>	<b>1.3</b>
<i>Of which:</i>								
Interest expenditure	3.3	3.5	3.7	3.6	3.7	3.8	3.9	3.9
Growth effect	0.7	0.3	-0.3	-0.3	-1.1	-0.8	-1.0	-1.3
Inflation effect	-0.8	0.0	0.0	-0.2	-1.1	-0.7	-1.0	-1.3
<b>3. Stock-flow adjustment</b>	<b>1.9</b>	<b>-1.6</b>	<b>0.2</b>	<b>0.2</b>	<b>0.0</b>	<b>-0.2</b>	<b>-0.2</b>	<b>0.0</b>
<i>Of which:</i>								
Cash/accruals diff.								
Acc. financial assets				0.6		0.6	0.6	0.3
<i>Privatisation</i>				0.6		0.6	0.6	0.3
Val. effect & residual								

Notes:

<sup>1</sup> End of period.

<sup>2</sup> The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

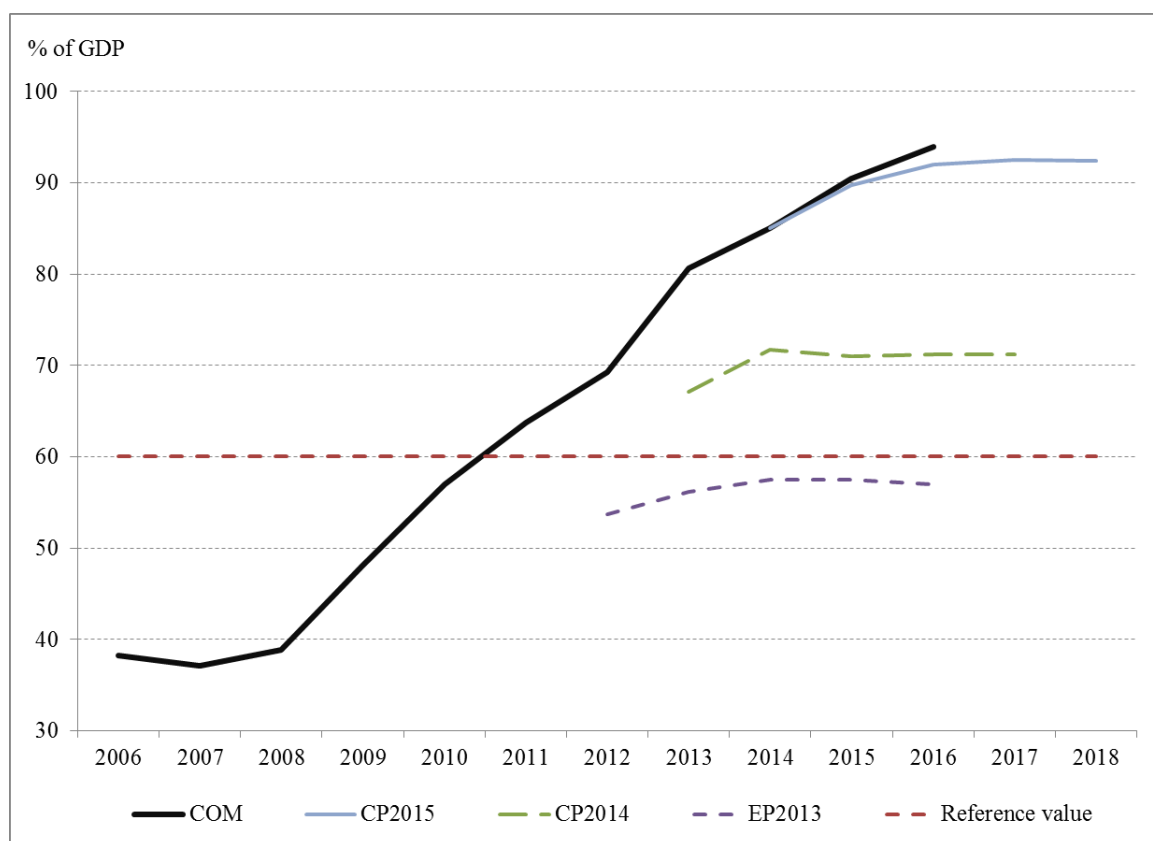
Source:

Commission 2015 spring forecast (COM); Convergence Programme (CP); Commission calculations.

Debt developments, as presented in the programme imply significant stock flow adjustments related to privatisations; in the period 2015-2018 the aggregate privatisation receipts should reach 2% of GDP. However, the programme does not sufficiently substantiate these receipts with concrete plans.<sup>6</sup>

<sup>6</sup> Two companies currently in the process of privatisation are mentioned: *Luka Vukovar* and *Imunološki Zavod*. (In the National Reform Programme, one more company is listed as a candidate for swift privatisation: *Končar elektroindustrija*.) In addition, three more companies are foreseen for soon privatisation: *Đuro Đaković Holding*, *Petrokemija* and *Hrvatska Poštanska Banka*.

**Figure 1: Government debt projections in successive programmes (% of GDP)**



Source: Commission 2015 spring forecast; Convergence Programmes.

### 3.4. Risk assessment

#### Deficit developments

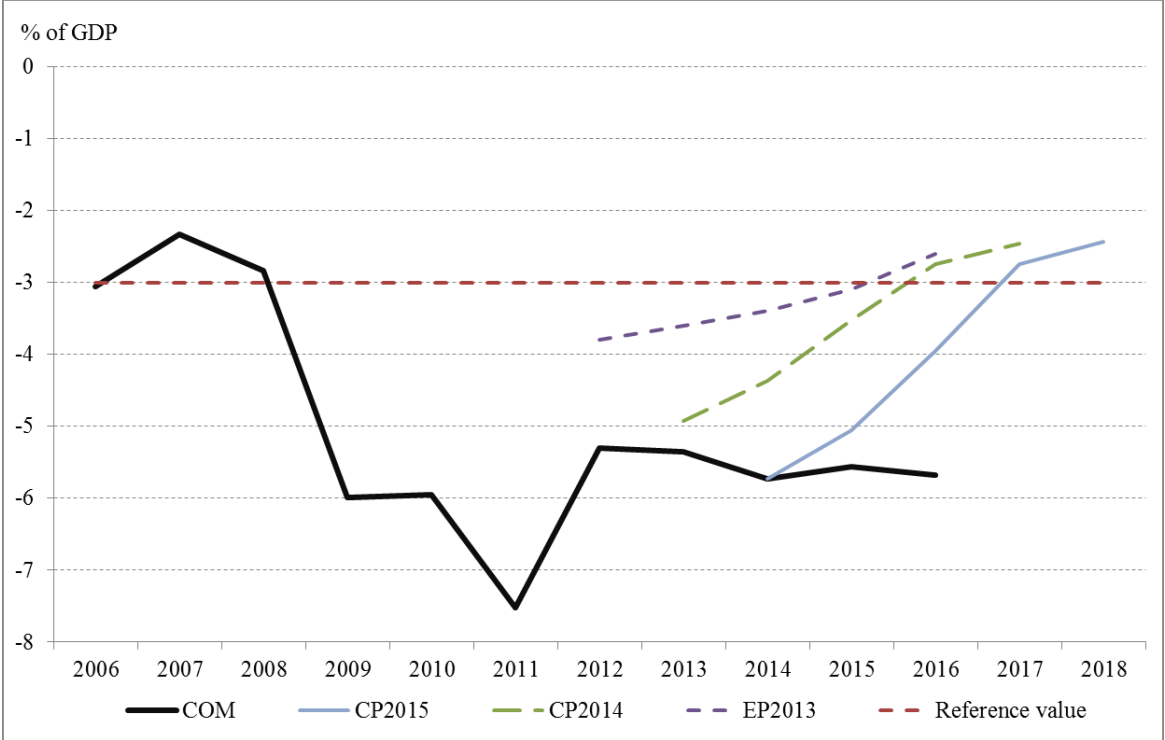
Macroeconomic and inflationary projections from the Convergence Programme for 2015 and 2016 seem somewhat favourable (the projected GDP growth figures are close to the Commission 2015 spring forecast, but implicitly assume a considerably larger consolidation effort). In 2017 and 2018, the authorities expect a slight acceleration of economic activity and moderate increase in inflation, which is broadly plausible.

There are considerable implementation risks to the measures reported in the programme for 2015 and 2016 (also related to the impact of the upcoming parliamentary elections). Revenue projections in 2015 and 2016 are slightly above the Commission forecast, reflecting among others a higher anticipated yield from current and past measures. However, the most substantial risks to the programme targets in 2015 and 2016 relate to the yield and implementation of the expenditure side measures. (see the discussion on the risks to the measures in the programme under Section 3.2). Moreover, strict enforcement mechanisms on the side of the central government appear to be missing, which increases the possibility that not all measures would be followed through. (see Section 6). In particular for the later years of the programme, there are no measures reported to achieve the targets.

Further risks relate to the continued generation of arrears in the health sector, as well as increased interest expenditure if market rates would go up from current historically low levels.

Additional risks relate to contingent liabilities, notably from numerous guarantees issued to SOEs, in particular to companies in road and railway transportation sectors. The recent example of an increase of the deficit in 2014 by 0.3% of GDP due to a 3<sup>rd</sup> call made against a loan issued to the railways' cargo operator is a case in point. The likelihood of these risks materialising also depends on the success of the restructuring operations of state-owned enterprises.

**Figure 2: Government balance projections in successive programmes (% of GDP)**



Source: Commission 2015 spring forecast; Convergence Programmes.

**Debt developments**

As mentioned above, debt projections in the programme rely on a significant privatisation programme (above 2% of GDP of stock-flow adjustment over 2015-2018), which does not seem to be substantiated by sufficiently specified privatisation plans.

Further, and apart from the risks related to the development of the deficit mentioned above (and in particular a potential call of guarantees), a specific source of concern is the currency structure of the Croatian public debt, which exposes its repayment to the foreign exchange risk (almost 80% of the public debt is denominated in the foreign currency). The sensitivity analysis reported in the Convergence Programme shows that a 15% depreciation of the kuna against the euro would lead to public debt rising above 103% of GDP in the period 2016-2018.

A deterioration of liquidity conditions on international financial markets or a significantly worsened market sentiment could further challenge Croatia's financing costs. In particular, the combination of high public and private debt stocks continues to make the economy vulnerable to negative economic shocks.

#### 4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

##### **Box 1. Council recommendations addressed to Croatia**

- On 28 January 2014, the Council recommended Croatia under Art. 126(7) of the Treaty to correct its excessive deficit by 2016. To this end, Croatia should reach a headline general government deficit target of 4.6 % of GDP in 2014, 3.5 % of GDP in 2015 and 2.7% of GDP in 2016, which is consistent with an annual improvement in the structural balance of 0.5 % of GDP in 2014, 0.9 % of GDP in 2015 and 0.7% of GDP in 2016, and use any windfall gains for deficit reduction. The Council set the deadline of 30 April 2014 for Croatia to take effective action and, in accordance with Article 3(4a) of Regulation (EC) No 1467/97, to report in detail on the consolidation strategy that it envisages in order to achieve the targets; thereafter the Croatian authorities should report on progress made in the implementation of these recommendations at least every six months until the excessive deficit has been fully corrected. Furthermore, the Council invited the Croatian authorities to: (i) carry out a thorough expenditure review with the objective of rationalising wage, social security and subsidy outlays and to provide sufficient fiscal space for the implementation of growth-enhancing expenditure, including co-financing of projects funded by the Union; (ii) further improve tax compliance and increase the efficiency of its tax administration, and (iii) improve the institutional framework of public finances, including by enhancing multi-annual budgetary programming, by strengthening the role and independence of the Fiscal Policy Committee, and by ensuring compliance with fiscal rules.
- On 8 July 2014, the Council addressed recommendations to Croatia in the context of the European Semester. In particular, in the area of public finances the Council recommended to Croatia to fully implement the budgetary measures adopted for 2014, reinforce the budgetary strategy, further specifying announced measures for 2015 and 2016, and consider additional permanent, growth-friendly measures in order to ensure a sustainable correction of the excessive deficit by 2016. At the same time, ensure that the structural adjustment effort as specified in the Council recommendation under the Excessive Deficit Procedure is delivered. Align programme projections with ESA standards and Stability and Growth Pact requirements. Take measures to reinforce control over expenditure. By March 2015, carry out a thorough expenditure review. Reinforce the budgetary planning process, in particular by improving the accuracy of macroeconomic and budgetary forecasts and strengthening the binding nature of the annual and medium-term expenditure ceilings and improve the design of fiscal rules. By October 2014, ground in law the newly established Fiscal Policy Commission, strengthen its independence from all budgetary authorities, broaden its mandate, in particular with respect to the monitoring of all fiscal rules and the ex ante and ex post assessment of forecasts, and ensure adequate resourcing. Building on plans outlined in the National Reform Programme, present a concrete strategy to reform recurrent property taxation. Initiate a process of reporting and reviewing of tax expenditures. Improve tax compliance, in particular by further enhancing the efficiency of the tax administration. Present an action plan to this end by the end of 2014.

After missing the headline deficit target in 2014, Croatia is again projected in the Commission 2015 spring forecast to miss the deficit target in 2015 (5.6% of GDP compared to 3.5% of GDP target). Moreover, a timely correction by 2016 is not ensured (projected deficit of 5.7% of GDP), nor is it planned in the Programme.

The change in the structural balance in 2014 is projected at -0.4% of GDP, which is 0.9% of GDP below the recommended 0.5% of GDP. This warrants a careful analysis.

The projected adjusted change in the structural balance amounts to 0.4% of GDP in 2014, slightly below the recommended effort of 0.5% of GDP, due to a much more pronounced shortfall in revenues in 2014 than expected, in particular in tax revenue. Based on the bottom-up assessment, the effort delivered by Croatia stands at 2.5% of GDP in 2014, exceeding the 2.3% of GDP of structural measures considered necessary to achieve the required fiscal effort.

The gap between the top-down and bottom-up assessment of the fiscal effort mainly stems from the downward revision in inflation in 2014. While at the time of the recommendation inflation was forecast to be 1.9%, it came out at 0%. Tax revenues are strongly impacted by low inflation. By comparison, public expenditures are less impacted by in-year revisions in inflation. The resulting deterioration in the headline balance is not corrected in the calculation of the structural balance, which takes into account the output gap only in real terms. Thus, the top-down assessment of the fiscal effort is sensitive to revisions in inflation. On the other side, the overall impact of the downward revision in inflation on the bottom-up assessment appears to be more limited.

In 2015 and 2016 the expected deterioration in the structural balance by 0.1% and 0.5% of GDP, respectively, falls short of the recommended efforts of 0.9% and 0.7% of GDP. The projected adjusted change in the structural balance stands at 0% and 0.6% of GDP in 2015 and 2016 respectively. From a bottom-up point of view, Croatia is not expected to achieve the required fiscal effort in 2015 nor in 2016, delivering 0.8% of GDP in 2015 and 0.5% of GDP in 2016, compared to the recommended 1% of GDP in both years. However, due to over-achieving the bottom-up effort in 2014 by 0.2% of GDP, the cumulative effort over 2014-2015 meets the target implied by the Council recommendation, at 3.3% of GDP.

Overall, based on the findings of the Commission 2015 spring forecast, Croatia has delivered the required fiscal effort over the period 2014-2015 based on the bottom-up approach, even if the fiscal effort remains below the recommended level in 2015 and further efforts will be needed for 2016.

**Table 4: Compliance with the requirements of the corrective arm**

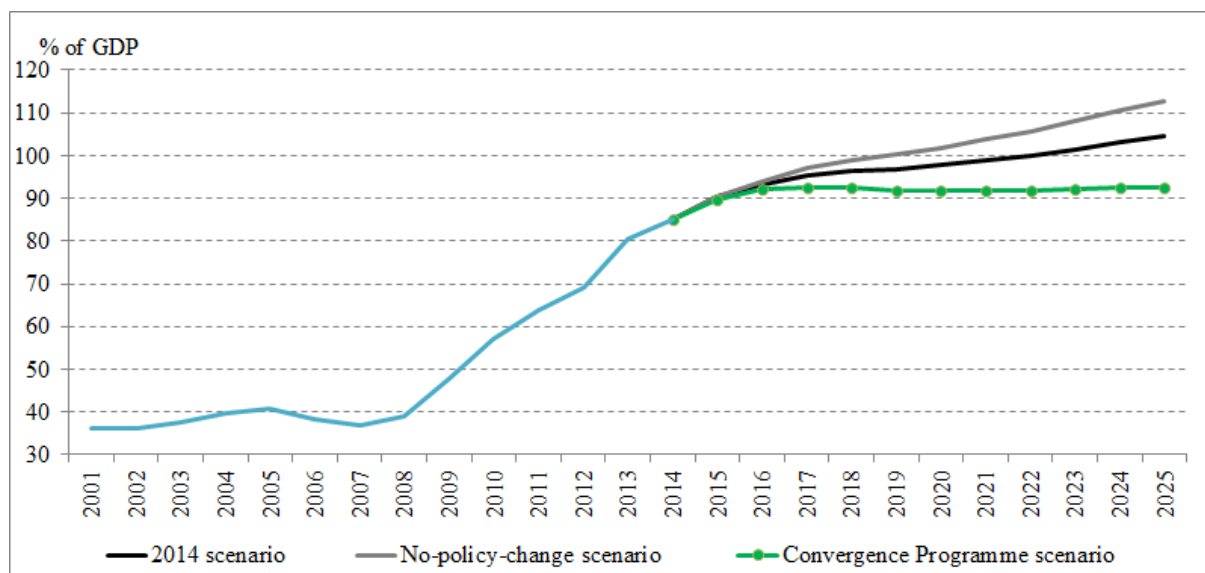
(% of GDP)	2014	2015		2016	
	COM	CP	COM	CP	COM
<b>Headline balance</b>					
Headline budget balance	-5.7	-5.0	-5.6	-3.9	-5.7
EDP requirement on the budget balance	-4.6	-3.5		-2.7	
<b>Fiscal effort - change in the structural balance</b>					
Change in the structural balance <sup>1</sup>	-0.4	0.4	-0.1	0.6	-0.5
Cumulative change <sup>2</sup>	-0.4	0.0	-0.5	0.7	-1.1
Required change from the EDP recommendation	0.5	0.9		0.7	
Cumulative required change from the EDP recommendation	0.5	1.4		2.1	
<b>Fiscal effort - adjusted change in the structural balance</b>					
Adjusted change in the structural balance <sup>3</sup>	0.4	-	0.0	-	0.6
of which:					
<i>correction due to change in potential GDP estimation (α)</i>	-0.1	-	0.2	-	0.5
<i>correction due to revenue windfalls/shortfalls (β)</i>	-0.8	-	0.1	-	-0.7
Cumulative adjusted change <sup>2</sup>	0.4	-	0.4	-	1.0
Required change from the EDP recommendation	0.5	0.9		0.7	
Cumulative required change from the EDP recommendation	0.5	1.4		2.1	
<b>Fiscal effort - calculated on the basis of measures (bottom-up approach)</b>					
Fiscal effort (bottom-up) <sup>4</sup>	2.5	-	0.8	-	0.5
Cumulative fiscal effort (bottom-up) <sup>2</sup>	2.5	-	3.3	-	3.9
Requirement from the EDP recommendation	2.3	1.0		1.0	
Cumulative requirement from the EDP recommendation	2.3	3.3		4.3	
Notes					
<sup>1</sup> Structural balance = cyclically-adjusted government balance excluding one-off measures. Structural balance based on the Convergence Programme are recalculated by the Commission on the basis of the programme scenario, using the commonly agreed methodology. Change compared to t-1.					
<sup>2</sup> Cumulated since the latest EDP recommendation.					
<sup>3</sup> Change in the structural balance corrected for unanticipated revenue windfalls/shortfalls and changes in potential growth compared to the scenario underpinning the EDP recommendations.					
<sup>4</sup> The estimated budgetary impact of the additional fiscal effort delivered on the basis of the discretionary revenue measures and the expenditure developments under the control of the government between the baseline scenario underpinning the EDP recommendation and the current forecast.					
<i>Source:</i>					
<i>Convergence Programme (CP); Commission 2015 spring forecast (COM); Commission calculations.</i>					



## 5. LONG-TERM SUSTAINABILITY

Government debt stood at 85% of GDP in 2014. It is expected to rise further to 92.5% in 2017 remaining above the 60% of GDP Treaty threshold (see Figure 3). However, the full implementation of the programme would broadly stabilise the debt ratio as of 2017, although remaining above the 60% of GDP reference value.

**Figure 3: Gross debt projections (% of GDP)**



Source: Commission calculations.

The analysis in this section includes the new long-term budgetary projections of age-related expenditure (pension, health care, long-term care, education and unemployment benefits) from the 2015 Ageing Report<sup>7</sup> published on 12 May. It therefore updates the assessment made in the Country Report<sup>8</sup> published on 26 February. Croatia appears to face low long-term fiscal sustainability risks, but faces higher risks in the medium-term. A low risk of fiscal stress in the short run is indicated in Table 5.

The medium-term sustainability gap is at 5.1 % of GDP, primarily related to the initial budgetary position and the high level of government debt (around 90% of GDP in 2015), indicating high risks. In the long-term, Croatia appears to face low fiscal sustainability risks. The long-term sustainability gap that shows the adjustment effort needed to ensure that the debt-to-GDP ratio is not on an ever-increasing path, is at -0.1% of GDP.

Risks would be lower in the event of the structural primary balance reverting to the lower values observed in the past, such as the average for the period 2004-2013. It is therefore appropriate for Croatia to continue to implement measures that reduce risks to fiscal sustainability in the short term and to reduce the government debt.

<sup>7</sup> See [http://ec.europa.eu/economy\\_finance/publications/european\\_economy/2015/ee3\\_en.htm](http://ec.europa.eu/economy_finance/publications/european_economy/2015/ee3_en.htm)

<sup>8</sup> See [http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index\\_en.htm](http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index_en.htm)

**Table 5: Sustainability indicators**

	Croatia			European Union		
	2014 scenario	No-policy-change scenario	Convergence Programme scenario	2014 scenario	No-policy-change scenario	Stability/Convergence Programme scenario
S2*	-0.9	-0.1	-2.5	1.4	1.7	0.4
<i>of which:</i>						
Initial budgetary position (IBP)	2.0	2.5	-0.2	0.4	0.5	-0.7
Long-term cost of ageing (CoA)	-2.8	-2.6	-2.3	1.0	1.1	1.1
<i>of which:</i>						
pensions	-2.9	-2.8	-2.6	0.0	0.1	0.1
healthcare	0.7	0.7	0.6	0.8	0.7	0.6
long-term care	0.0	0.0	0.0	0.7	0.7	0.6
others	-0.6	-0.5	-0.3	-0.4	-0.3	-0.2
S1**	3.7	5.1	3.1	1.4	1.8	0.5
<i>of which:</i>						
Initial budgetary position (IBP)	3.1	3.5	0.9	-0.4	-0.3	-1.6
Debt requirement (DR)	1.4	2.2	2.4	1.7	1.9	1.8
Long-term cost of ageing (CoA)	-0.8	-0.5	-0.2	0.1	0.3	0.4
S0 (risk for fiscal stress)***	0.20	:	:	:	:	:
<i>Fiscal subindex</i>	0.30	:	:	:	:	:
<i>Financial-competitiveness subindex</i>	0.16	:	:	:	:	:
Debt as % of GDP (2014)	85.0			88.6		
Age-related expenditure as % of GDP (2014)	22.1			25.6		
Source: Commission, 2015 Convergence Programme						
Note: the '2014' scenario depicts the sustainability gap under the assumption that the structural primary balance position remains at the 2014 position according to the Commission 2015 spring forecast; the 'no-policy-change' scenario depicts the sustainability gap under the assumption that the structural primary balance position evolves according to the Commission 2015 spring forecast until 2016. The 'stability programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented over the period covered by the programme. Age-related expenditure as given in the 2015 Ageing Report.						
* The long-term sustainability gap (S2) indicator shows the immediate and permanent adjustment required to satisfy an inter-temporal budgetary constraint, including the costs of ageing. The S2 indicator has two components: i) the initial budgetary position (IBP) which gives the gap to the debt stabilising primary balance; and ii) the additional adjustment required due to the costs of ageing. The main assumption used in the derivation of S2 is that in an infinite horizon, the growth in the debt ratio is bounded by the interest rate differential (i.e. the difference between the nominal interest and the real growth rates); thereby not necessarily implying that the debt ratio will fall below the EU Treaty 60% debt threshold. The following thresholds for the S2 indicator were used: (i) if the value of S2 is lower than 2, the country is assigned low risk; (ii) if it is between 2 and 6, it is assigned medium risk; and, (iii) if it is greater than 6, it is assigned high risk.						
** The medium-term sustainability gap (S1) indicator shows the upfront adjustment effort required, in terms of a steady adjustment in the structural primary balance to be introduced over the five years after the forecast horizon, and then sustained, to bring debt ratios to 60% of GDP in 2030, including financing for any additional expenditure until the target date, arising from an ageing population. The following thresholds were used to assess the scale of the sustainability challenge: (i) if the S1 value is less than zero, the country is assigned low risk; (ii) if a structural adjustment in the primary balance of up to 0.5 p.p. of GDP per year for five years after the last year covered by the spring 2015 forecast (year 2016) is required (indicating an cumulated adjustment of 2.5 pp.), it is assigned medium risk; and, (iii) if it is greater than 2.5 (meaning a structural adjustment of more than 0.5 p.p. of GDP per year is necessary), it is assigned high risk.						
*** The S0 indicator reflects up to date evidence on the role played by fiscal and financial-competitiveness variables in creating potential fiscal risks. It should be stressed that the methodology for the S0 indicator is fundamentally different from the S1 and S2 indicators. S0 is not a quantification of the required fiscal adjustment effort like the S1 and S2 indicators, but a composite indicator which estimates the extent to which there might be a risk for fiscal stress in the short-term. The critical threshold for the overall S0 indicator is 0.43. For the fiscal and the financial-competitiveness sub-indexes, thresholds are respectively at 0.35 and 0.45.						

## **6. FISCAL FRAMEWORK AND QUALITY OF PUBLIC FINANCES<sup>9</sup>**

### **6.1. Fiscal framework**

Challenges in the Croatian fiscal framework relate to the independence of the Fiscal policy commission and the revision of the Fiscal Responsibility Act, the improvement of numerical fiscal rules, expenditures' control and budgetary planning.

The implementation of the 2014 country specific recommendations in this area recorded only modest progress: most of the measures regarding the budgetary planning process, design of the fiscal rules and independence of the Fiscal Policy Commission, although announced, have not yet been adopted.

Amendments to the Budget Act have been adopted in February 2015. The new act is bringing a number of improvements to the Croatian budgetary framework. The budgetary process is now harmonised with the timeline of the European Semester, including the submission dates for the Convergence Programme and the National Reform Programme. Economic and Fiscal Policy Guidelines are clearly identified as the medium-term budgetary anchor. There is a reference to ESA2010 as a standard for the application of the act. Additional transparency has been introduced, by differentiating budget limits for existing and new activities. This should enable more realistic expenditure planning, because introducing the new programmes will not be allowed if the existing programmes are not fully covered by the available funds. Also, there is a provision that enables the reallocation of the funds to ensure the co-financing of the EU funded projects. Finally, the now obsolete provision setting public debt limitations in the previous regulation (which prohibited any increase of the public debt, as long as the public debt-to GDP ratio is above 60%) is abolished, while it is stipulated to publicly set out a public debt strategy starting as of 2016, on a three-year basis.

### **6.2. Quality of public finances**

The Convergence Programme announces some positive measures for the management of public finances, such as changes in the Act on internal financial control and the Fiscal responsibility act, and the issuance of binding opinions by the Tax authorities. Also, the programme envisages a strengthened role for the State Audit Office, but it is not clear how and when this will be done. Fiscal risks related to the healthcare and pension system remain in spite of the planned changes that should enable more efficient use of public funds.

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<sup>9</sup> This section complements the Country Report published on 26 February 2015 and updates it with the information included in the Convergence programme.

## **7. CONCLUSIONS**

In 2014, Croatia achieved a headline deficit of 5.7% of GDP, 1.1% of GDP above the target under the EDP recommendation. However, the fiscal effort has been delivered on the basis of the bottom-up method.

Croatia plans to correct its excessive deficit by 2017, one year later than the 2016 deadline set by the Council. The programme is based on somewhat favourable growth assumptions, which – in combination with implementation risks to the budgetary measures – pose risks to meeting the headline targets, although they remain within reach.

Based on the Commission 2015 spring forecast, the headline deficit is expected to decrease to 5.6% of GDP in 2015 but then (on a no-policy-change basis) increase again to 5.7% of GDP in 2016.

Overall, on the basis of the findings of the Commission 2015 spring forecast, the fiscal effort delivered by Croatia is in line with what was recommended by the Council over the period 2014-2015, based on the bottom-up approach, even if the fiscal effort remains below the recommended level in 2015 and further efforts will be required for 2016.

## ANNEX

Table I. Macroeconomic indicators

	1997-2001	2002-2006	2007-2011	2012	2013	2014	2015	2016
<b>Core indicators</b>								
GDP growth rate	3.0	4.8	-0.4	-2.2	-0.9	-0.4	0.3	1.2
Output gap <sup>1</sup>	-2.5	1.2	2.1	-2.6	-3.2	-3.5	-3.2	-2.1
HICP (annual % change)	4.3	2.7	2.8	3.4	2.3	0.2	0.1	1.3
Domestic demand (annual % change) <sup>2</sup>	2.9	6.3	-1.2	-3.3	-0.9	-1.8	-0.3	0.8
Unemployment rate (% of labour force) <sup>3</sup>	14.4	13.6	10.6	16.0	17.3	17.3	17.0	16.6
Gross fixed capital formation (% of GDP)	20.8	25.2	24.3	19.6	19.3	18.6	18.1	18.1
Gross national saving (% of GDP)	17.9	22.2	21.2	19.2	18.9	18.4	19.3	20.4
<b>General Government (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>n.a</b>	<b>n.a</b>	<b>-7.5</b>	<b>-5.3</b>	<b>-5.4</b>	<b>-5.7</b>	<b>-5.6</b>	<b>-5.7</b>
<b>Gross debt</b>	<b>36.1</b>	<b>38.5</b>	<b>48.9</b>	<b>69.2</b>	<b>80.6</b>	<b>85.0</b>	<b>90.5</b>	<b>93.9</b>
<b>Net financial assets</b>	<b>15.1</b>	<b>5.0</b>	<b>-1.2</b>	<b>-16.2</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Total revenue	n.a	n.a	41.0	41.7	42.4	42.3	42.7	42.9
Total expenditure	n.a	n.a	48.5	47.0	47.7	48.0	48.3	48.6
<i>of which: Interest</i>	n.a	n.a	3.0	3.4	3.5	3.5	3.7	3.7
<b>Corporations (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>n.a</b>	<b>-3.9</b>	<b>-1.8</b>	<b>0.6</b>	<b>2.9</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
<b>Net financial assets; non-financial corporations</b>	<b>-100.3</b>	<b>-105.0</b>	<b>-143.3</b>	<b>-150.0</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
<b>Net financial assets; financial corporations</b>	<b>1.1</b>	<b>-5.2</b>	<b>-4.6</b>	<b>4.9</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Gross capital formation	n.a	18.1	16.8	12.3	12.1	n.a	n.a	n.a
Gross operating surplus	n.a	18.5	20.0	18.6	18.3	n.a	n.a	n.a
<b>Households and NPISH (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>n.a</b>	<b>2.5</b>	<b>2.3</b>	<b>5.0</b>	<b>3.0</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
<b>Net financial assets</b>	<b>55.2</b>	<b>47.1</b>	<b>54.5</b>	<b>64.2</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Gross wages and salaries	n.a	43.2	43.7	43.9	44.1	n.a	n.a	n.a
Net property income	n.a	1.1	1.2	1.7	1.2	n.a	n.a	n.a
Current transfers received	n.a	19.1	17.8	19.1	17.3	n.a	n.a	n.a
Gross saving	n.a	6.1	6.2	8.2	6.3	n.a	n.a	n.a
<b>Rest of the world (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>-4.3</b>	<b>-5.6</b>	<b>-4.5</b>	<b>0.0</b>	<b>0.1</b>	<b>0.6</b>	<b>1.8</b>	<b>2.8</b>
<b>Net financial assets</b>	<b>29.4</b>	<b>58.2</b>	<b>95.1</b>	<b>97.8</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Net exports of goods and services	-6.5	-6.8	-4.0	0.5	0.5	2.1	3.0	3.4
Net primary income from the rest of the world	-1.3	-2.3	-2.8	-3.1	-1.9	-3.0	-2.7	-2.6
Net capital transactions	n.a	0.0	0.0	0.0	0.0	-0.1	-0.2	-0.1
Tradable sector	46.8	46.0	43.3	43.2	43.1	43.1	n.a	n.a
Non tradable sector	36.9	38.1	42.3	41.7	41.6	41.5	n.a	n.a
<i>of which: Building and construction sector</i>	5.1	6.1	6.4	4.7	4.5	4.3	n.a	n.a
Real effective exchange rate (index, 2000=100)	82.5	89.3	98.9	92.6	91.5	88.4	83.7	83.5
Terms of trade goods and services (index, 2000=100)	88.1	93.4	99.0	99.6	99.7	100.1	100.7	100.7
Market performance of exports (index, 2000=100)	99.3	113.5	103.0	100.1	102.0	104.8	104.4	103.8
<b>Notes:</b>								
<sup>1</sup> The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.								
<sup>2</sup> The indicator on domestic demand includes stocks.								
<sup>3</sup> Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.								
<i>Source:</i>								
AMECO data, Commission 2015 spring forecast.								