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NOTE

From:	General Secretariat of the Council
To:	Permanent Representatives Committee/Council
Subject:	COUNCIL RECOMMENDATION on the economic, social, employment, structural and budgetary policies of Croatia

Delegations will find attached the above-mentioned draft Council Recommendation, as revised and agreed by various Council committees and finalized by the Economic and Financial Committee, based on the Commission Proposal COM(2025) 211 final.

COUNCIL RECOMMENDATION

on the economic, social, employment, structural and budgetary policies of Croatia

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 121(2) and Article 148(4) thereof,

Having regard to Regulation (EU) 2024/1263 of the European Parliament and of the Council of 29 April 2024 on the effective coordination of economic policies and on multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97[1], and in particular Article 3(3) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

[1] OJ L, 2024/1263, 30.4.2024, ELI: http://data.europa.eu/eli/reg/2024/1263/oj.

Whereas:

General considerations

(1) Regulation (EU) 2024/1263, which entered into force on 30 April 2024, specifies the objectives of the economic governance framework, which aims at promoting sound and sustainable public finances and sustainable and inclusive growth and resilience through reforms and investments, and preventing excessive government deficits. The Regulation stipulates that the Council and the Commission conduct multilateral surveillance in the context of the European Semester in accordance with the objectives and requirements set out in the TFEU. The European Semester includes, in particular, the formulation, and the surveillance of the implementation of country-specific recommendations. The Regulation also promotes national ownership of fiscal policy and emphasises its medium-term focus, combined with more effective and coherent enforcement. Each Member State must submit to the Council and the Commission a national medium-term fiscal-structural plan, containing its fiscal, reform and investment commitments, over 4 or 5 years, depending on the length of the national legislative term. The net expenditure[2] path in these plans has to comply with the Regulation's requirements, including the requirements to put or keep general government debt on a plausibly downward path by the end of the adjustment period, or for it to remain at prudent levels below 60% of gross domestic product (GDP), and to bring and/or maintain the general government deficit below the 3%-of-GDP Treaty reference value over the medium term. Where a Member State commits to a relevant set of reforms and investments in accordance with the criteria set out in the Regulation, the adjustment period may be extended by up to three years.

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[2] Net expenditure as defined in Article 2, point (2), of Regulation (EU) 2024/1263: 'net expenditure' means government expenditure net of (i) interest expenditure; (ii) discretionary revenue measures; (iii) expenditure on programmes of the Union fully matched by revenue from Union funds; (iv) national expenditure on co-financing of programmes funded by the Union; (v) cyclical elements of unemployment benefit expenditure; and (vi) one-offs and other temporary measures.

(2) Regulation (EU) 2021/241 of the European Parliament and of the Council[3], which established the Recovery and Resilience Facility (the 'RRF'), entered into force on 19 February 2021. The RRF provides financial support to Member States for implementing reforms and investments, delivering a fiscal impulse financed by the Union. In line with the priorities of the European Semester for economic policy coordination, the RRF fosters economic and social recovery while driving sustainable reforms and investments, in particular promoting the green and digital transitions and making Member States' economies more resilient. It also helps strengthen public finances and boost growth and job creation in the medium and long term, improve territorial cohesion within the Union and support the continued implementation of the European Pillar of Social Rights.

(3) Regulation (EU) 2023/435 of the European Parliament and of the Council[4] (the 'REPowerEU Regulation'), which was adopted on 27 February 2023, aims to phase out the Union's dependence on Russian fossil-fuel imports. This helps achieve energy security and diversify the Union's energy supply, while increasing the uptake of renewables, energy storage capacities and energy efficiency. Croatia added a new REPowerEU chapter to its national recovery and resilience plan in order to finance key reforms and investments that will help achieve the REPowerEU objectives.

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[3] 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, ELI: http://data.europa.eu/eli/reg/2021/241/oj).

[4] 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, ELI: http://data.europa.eu/eli/reg/2023/435/oj).

(4) On 15 May 2021, Croatia submitted its national recovery and resilience plan to the Commission, in accordance with Article 18(1) of Regulation (EU) 2021/241. Pursuant to Article 19 of that Regulation, the Commission assessed the relevance, effectiveness, efficiency and coherence of the recovery and resilience plan, in accordance with the assessment guidelines set out in Annex V. On 28 July 2021, the Council adopted its Implementing Decision approving the assessment of the recovery and resilience plan for Croatia[5], which was amended under Article 18(2) on 7 December 2023 to update the maximum financial contribution for non-repayable financial support, as well as to include the REPowerEU chapter[6]. The release of instalments is conditional on the adoption of a decision by the Commission, in accordance with Article 24(5), stating that Croatia has satisfactorily achieved the relevant milestones and targets set out in the Council Implementing Decision. Satisfactory achievement requires that the achievement of preceding milestones and targets for the same reform or investment has not been reversed.

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[5] Council Implementing Decision of 28 July 2021 on the approval of the assessment of the recovery and resilience plan for Croatia (ST 10687/2021).

[6] Council Implementing Decision of 7 December 2023 amending the Implementing Decision of 28 July 2021 on the approval of the assessment of the recovery and resilience plan for Croatia (ST 15834/2023).

(5) On 21 January 2025 the Council, upon the recommendation of the Commission, adopted a recommendation endorsing the national medium-term fiscal-structural plan of Croatia[7]. The plan was submitted in accordance with Article 11 and Article 36(1), point (a), of Regulation (EU) 2024/1263, covers the period from 2025 until 2028 and presents a fiscal adjustment spread over four years.

(6) On 26 November 2024, the Commission adopted an opinion on the 2025 draft budgetary plan of Croatia. On the same date, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the 2025 Alert Mechanism Report, in which it did not identify Croatia as one of the Member States for which an in-depth review would be needed. The Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area and a proposal for the 2025 Joint Employment Report, which analyses the implementation of the Employment Guidelines and the principles of the European Pillar of Social Rights. The Council adopted the Recommendation on the economic policy of the euro area[8] on 13 May 2025 and the Joint Employment Report on 10 March 2025.

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[7] Council Recommendation of 21 January 2025 endorsing the medium-term fiscal-structural plan of Croatia OJ C/2025/638, 10.2.2025.

[8] Council Recommendation of 13 May 2025 on the economic policy of the euro area (OJ C, C/2025/2782, 22.5.2025, ELI: http:// data.europa.eu/eli/C/2025/2782/oj).

(7) On 29 January 2025, the Commission published the Competitiveness Compass, a strategic framework that aims to boost the EU's global competitiveness over the next five years. It identifies the three transformative imperatives of sustainable economic growth: (i) innovation; (ii) decarbonisation and competitiveness; and (iii) security. To close the innovation gap, the EU aims to foster industrial innovation, support the growth of start-ups through initiatives like the EU Start-up and Scale-up Strategy, and promote the adoption of advanced technologies like artificial intelligence and quantum computing. In pursuit of a greener economy, the Commission has outlined a comprehensive Affordable Energy Action Plan and a Clean Industrial Deal, ensuring that the shift to clean energy remains cost-effective, competitiveness-friendly, particularly for energy-intensive sectors, and is a driver for growth. To reduce excessive dependencies and increase security, the Union is committed to strengthening global trade partnerships, diversifying supply chains and securing access to critical raw materials and clean energy sources. These priorities are underpinned by horizontal enablers, namely regulatory simplification, deepening of the single market, financing competitiveness and a Savings and Investments Union, promotion of skills and quality jobs, and better coordination of EU policies. The Competitiveness Compass is aligned with the European Semester, ensuring that Member States' economic policies are consistent with the Commission's strategic objectives, creating a unified approach to economic governance that fosters sustainable growth, innovation and resilience across the Union.

(8) In 2025, the European Semester for economic policy coordination continues to develop alongside the implementation of the RRF. The full implementation of the recovery and resilience plans remains essential for delivering on the policy priorities under the European Semester, as the plans help effectively address all or a significant subset of challenges identified in the relevant country-specific recommendations issued in recent years. These country-specific recommendations remain equally relevant for the assessment of amended recovery and resilience plans in accordance with Article 21 of Regulation (EU) 2021/241.

(9) The 2025 country-specific recommendations cover the key economic policy challenges that are not sufficiently addressed by measures included in the recovery and resilience plans, taking into account the relevant challenges identified in the 2019-2024 country-specific recommendations.

(10) On 4 June 2025, the Commission published the 2025 country report for Croatia. It assessed Croatia's progress in addressing the relevant country-specific recommendations and took stock of Croatia's implementation of the recovery and resilience plan. Based on this analysis, the country report identified the most pressing challenges Croatia is facing. It also assessed Croatia's progress in implementing the European Pillar of Social Rights and in achieving the Union's 2030 headline targets on employment, skills and poverty and social exclusion reduction, as well as progress in achieving the United Nations Sustainable Development Goals.

Assessment of the Annual Progress Report

(11) On 21 January 2025 the Council recommended the following maximum growth rates of net expenditure for Croatia: 6.4% in 2025, 4.9% in 2026, 4.1% in 2027, and 3.7% in 2028, which correspond to the maximum cumulative growth rates calculated by reference to 2023 of 26.2% in 2025, 32.3% in 2026, 37.8% in 2027, and 42.9% in 2028. On 22 May 2025 Croatia submitted its Annual Progress Report[9], on adherence to the recommended maximum growth rates of net expenditure and the implementation of reforms and investments responding to the main challenges identified in the European Semester country-specific recommendations. The Annual Progress Report also reflects Croatia's biannual reporting on the progress made in achieving its recovery and resilience plan in accordance with Article 27 of Regulation (EU) 2021/241.

(12) Russia's war of aggression against Ukraine and its repercussions constitute an existential challenge for the European Union. The Commission recommended to activate the national escape clause of the Stability and Growth Pact in a coordinated manner to support the EU efforts to achieve a rapid and significant increase in defence spending and this proposal was welcomed by the European Council of 6 March 2025. Following the request of Croatia on 27 May 2025, on [date; OJ: please insert here as date 8 July 2025] the Council, upon the recommendation of the Commission, adopted a recommendation allowing Croatia to deviate from, and exceed, the recommended maximum growth rates of net expenditure[10].

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9 The 2025 Annual Progress Reports are available on: https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/stability-and-growth-pact/preventive-arm/annual-progress-reports_en.

10 Council recommendation allowing Croatia to deviate from the maximum growth rates of net expenditure as set by the Council under Regulation (EU) 2024/1263 (Activation of the national escape clause), OJ [OJ: please insert in this footnote the reference and date of adoption of Council Recommendation contained in document ST 10470/25]

(13) Based on data validated by Eurostat[11], Croatia's general government deficit increased from 0.8% of GDP in 2023 to 2.4% in 2024, while the general government debt fell from 61.8% of GDP at the end of 2023 to 57.6% at the end of 2024. According to the Commission's calculations, these developments correspond to a net expenditure growth rate of 17.4% in 2024. In the 2025 Annual Progress Report, Croatia estimates the net expenditure growth in 2024 at 17.5%. Based on the Commission's estimates, the fiscal stance[12], which includes both nationally and EU financed expenditure, was expansionary, by 1.8% of GDP, in 2024.

(14) According to the Annual Progress Report, the macroeconomic scenario underpinning the budgetary projections by Croatia expects real GDP growth at 3.3% in 2025, while CPI inflation is projected at 2.9% in 2025. The Commission Spring 2025 Forecast projects real GDP to grow by 3.2% in 2025 and 2.9% in 2026, and HICP inflation to stand at 3.4% in 2025 and 2.0% in 2026.

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[11] Eurostat-Euro Indicators, 22.4.2025.

[12] The fiscal stance is defined as a measure of the annual change in the underlying budgetary position of the general government. It aims to assess the economic impulse stemming from fiscal policies, both those that are nationally financed and those that are financed by the EU budget. The fiscal stance is measured as the difference between (i) the medium-term potential growth and (ii) the change in primary expenditure net of discretionary revenue measures and including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other Union funds.

(15) In the Annual Progress Report, the general government deficit is expected to increase to 2.9% of GDP in 2025, while the general government debt-to-GDP ratio is set to decrease to 56.9% by the end of 2025. These developments correspond to net expenditure growth of 7.6% in 2025. The Commission Spring 2025 Forecast projects a general government deficit of 2.7% of GDP in 2025. The increase of the deficit in 2025 mainly reflects a strong growth of capital expenditure supported by an expected step up in RRF implementation, carry over effect of the public sector wage reform and a further increase in pensions expenditure due to the change in the indexation formula. According to the Commission's calculations, these developments correspond to net expenditure growth of 7.9% in 2025. Based on the Commission's estimates, the fiscal stance, which includes both nationally and EU financed expenditure, is projected to be expansionary, by 0.8% of GDP, in 2025. The general government debt-to-GDP ratio is set to decrease to 56.3% by the end of 2025. The decrease of the debt-to-GDP ratio in 2025 mainly reflects the denominator effect from the expected nominal GDP growth.

(16) General government expenditure amounting to 1.8% of GDP is expected to be financed by non-repayable support ("grants") from the Recovery and Resilience Facility in 2025, compared to 0.9% of GDP in 2024, according to the Commission Spring 2025 Forecast. Expenditure financed by Recovery and Resilience Facility non-repayable support enables high-quality investment and productivity-enhancing reforms without a direct impact on the general government balance and debt of Croatia.

(17) General government defence expenditure in Croatia amounted to 1.0% of GDP in 2021, 1.0% of GDP in 2022 and 1.3% of GDP in 2023[13]. According to the Commission Spring 2025 Forecast, expenditure on defence is projected at 1.4% of GDP in 2024 and 1.5% of GDP in 2025. This corresponds to an increase of 0.5 percentage points of GDP compared to 2021. The period when the national escape clause is activated (2025-2028) allows Croatia to reprioritise government expenditure or increase government revenue so that lastingly higher defence expenditure would not endanger fiscal sustainability in the medium term.

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13 Eurostat, government expenditure by classification of functions of government (COFOG). Due to methodological differences between the COFOG and NATO definitions, expenditure based on the COFOG definition may differ from the expenditure based on the NATO definition.

(18) According to the Commission Spring 2025 Forecast, net expenditure in Croatia is projected to grow by 7.9% in 2025 and 26.6% cumulatively in 2024 and 2025. Based on the Commission Spring 2025 Forecast, the net expenditure growth of Croatia in 2025 is projected to be above the recommended maximum growth rate, corresponding to a deviation[14] of 0.6% of GDP in annual terms. When considering 2024 and 2025 together, the cumulative growth rate of net expenditure is also projected to be above the recommended maximum growth rate, corresponding to a deviation of 0.2% of GDP. However, the projected deviation is within the flexibility of the national escape clause based on current projections for defence spending.

(19) The Annual Progress Report does not include budgetary projections beyond 2025. Based on policy measures known at the cut-off date of the forecast, the Commission Spring 2025 Forecast projects a general government deficit of 2.6% of GDP in 2026. These developments correspond to net expenditure growth of 4.9% in 2026. Based on the Commission's estimates, the fiscal stance, which includes both nationally and EU financed expenditure, is projected to be broadly neutral in 2026. The general government debt-to-GDP ratio is projected by the Commission to increase to 56.4% by the end of 2026. The increase of the debt-to-GDP ratio in 2026 mainly reflects debt-increasing stock-flow adjustments.

[14] From 2026 these figures will appear in the control account that is established in Article 22 of the Regulation (EU) 2024/1263.

Key policy challenges

(20) In accordance with Article 19(3), point (b), of Regulation (EU) 2021/241 and criterion 2.2 of Annex V to that Regulation, the recovery and resilience plan includes an extensive set of mutually reinforcing reforms and investments to be implemented by 2026. These are expected to help effectively address all or a significant subset of challenges identified in the relevant country-specific recommendations. Within this tight timeframe, finalising the effective implementation of the recovery and resilience plan is essential to boost Croatia's long-term competitiveness through the green and digital transitions, while ensuring social fairness. The Commission Communication NextGenerationEU – The road to 2026, adopted on 4 June 2025, clarifies the applicable timeline for the end of the Facility and provides guidance to Member States to maximise implementation by 31 August 2026, including on how to further streamline their RRPs, lays out key options to consider when revising them, and stresses the importance of careful joint planning ahead for the submission of the last payment requests in 2026. Croatia has already made progress in implementing the reforms and investments in its Recovery and Resilience Plan. To deliver on the commitments of the recovery and resilience plan by August 2026, it is essential for Croatia to accelerate the implementation of reforms and investments by addressing relevant challenges in terms of administrative capacity constraints, complex public procurement procedures, protracted permitting processes and by improving coordination. The systematic involvement of local and regional authorities, social partners, civil society and other relevant stakeholders remains essential in order to ensure broad ownership for the successful implementation of the recovery and resilience plan.

(21) The implementation of cohesion policy programmes, which encompass support from the European Regional Development Fund (ERDF), the Just Transition Fund (JTF), the European Social Fund Plus (ESF+) and the Cohesion Fund (CF), has accelerated in Croatia. It is important to continue efforts to ensure the swift implementation of these programmes, while maximising their impact on the ground. Croatia is already taking action under its cohesion policy programmes to boost competitiveness and growth while enhancing social cohesion. At the same time, Croatia continues to face challenges, including those relating to enhancing competitiveness and innovation performance, affordable housing, water resilience, active labour market policies for disadvantaged groups, up- and reskilling, long-term care and deinstitutionalisation. In accordance with Article 18 of Regulation (EU) 2021/1060, Croatia is required – as part of the mid-term review of the cohesion policy funds – to review each programme taking into account, among other things, the challenges identified in the 2024 country-specific recommendations. The Commission proposals adopted on 1 April 2025[15] extend the deadline for submitting an assessment – for each programme – of the outcome of the mid-term review beyond 31 March 2025. They also provide flexibilities to help speed up programme implementation and incentives for Member States to allocate cohesion policy resources to five strategic priority areas of the Union, namely competitiveness in strategic technologies, defence, housing, water resilience and energy transition, and to investments in skills in priority sectors while maintaining the focus on persons in most vulnerable situations in ESF+ programmes.

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[15] Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulations (EU) 2021/1058 and (EU) 2021/1056 as regards specific measures to address strategic challenges in the context of the mid-term review − COM(2025) 123 final.

(22) The Strategic Technologies for Europe Platform (STEP) provides the opportunity to invest in a key EU strategic priority by strengthening the EU's competitiveness. STEP is channelled through 11 existing EU funds. Member States can also contribute to the InvestEU programme supporting investments in priority areas. Croatia could use these initiatives to support the development or manufacturing of critical technologies, including clean and resource-efficient technologies.

(23) Beyond the economic and social challenges addressed by the recovery and resilience plan and other EU funds, Croatia should effectively address the challenges related to labour and skills shortages, decarbonisation and energy efficiency, innovation, access to diversified sources of financing, the business environment and social inclusion.

(24) Croatia's research and innovation (R&I) performance continues to improve, but progress is hindered by persistent structural challenges, in particular the highly fragmented public research, development and innovation sector, which consists of numerous public research institutes and faculties within universities. The large number of these entities dilutes resources and hinders collaboration, resulting in lower research outputs and reduced scope for business-academia collaboration and technology transfer. Although Croatia has been implementing reforms under the recovery and resilience plan to reduce the number of public research institutions, increasing the scope, ambition and pace of implementation of these efforts would be beneficial. The level of public R&D expenditure as a share of GDP remains under EU average and has been stagnating in recent years. The share of business expenditure for R&D and the uptake of innovation schemes by businesses also remains well below the EU average, contributing to a suboptimal performance.

(25) Croatia's financing landscape is still predominantly supported by banks, with market-based finance playing a comparatively smaller role. Firms continue to rely heavily on internal funds and bank loans, while access to household savings via capital markets remains limited due to still low levels of direct retail participation, despite some progress. Domestic institutional investors, such as pension funds and insurers, assume a limited role in financing innovative businesses. The relatively small size and liquidity of the domestic capital markets limit exit options for venture capital and private equity investors, compounding the financing gap for innovative firms. Reforms under the recovery and resilience plan and the capital markets development strategy seek to promote regional integration, digitalisation, and diversification of financing options. Further progress is needed in boosting venture capital, private equity and financial literacy, and improving the investment environment.

(26) As set in the Competitiveness Compass, all the EU, national, and local institutions must make a major effort to produce simpler rules and to accelerate the speed of administrative procedures. The Commission has set ambitious goals for reducing administrative burden: by at least 25% and by at least 35% for SMEs. It has also created new tools to achieve these goals, including systematic stress test of the stock of EU legislation and enhanced stakeholders' dialogue. To match this ambition, Croatia also needs to take action. The complexity of administrative procedures is reported to be a constraint by 66% of companies when doing business in Croatia[16]. Structural challenges continue to weigh on Croatia's business environment, with labour and skills shortages, regulatory complexity, and administrative inefficiencies acting as major constraints on investment and growth. Regulatory barriers in sectors such as retail and in certain professions restrict competition, while delays in transposing EU directives increase uncertainty and compliance burdens for businesses. Measures in the recovery and resilience plan to digitalise public administration, promote competition, and simplify procedures are significant steps forward. However, increasing the scope, ambition and pace of regulatory simplification and administrative modernisation would be beneficial.

[16] 'Businesses' attitudes towards corruption in the EU' Flash Report, Eurobarometer Report (April 2024)

(27) The territorial fragmentation of Croatia's public administration affects its efficiency and exacerbates regional disparities. There is also an imbalance between responsibilities and resources at local level. This contributes to the uneven quality of public services provided across the country and raises administrative costs as many small local governments lack adequate financial and administrative resources to provide services within their remit. Although measures under the recovery and resilience plan help address the high fragmentation by providing financial incentives to stimulate mergers of local government units, the uptake of these incentives remains mainly focused on mergers of functions, while the uptake in terms of actual mergers of local government units remains limited. Increasing the scope of incentives, coupled with potential legislative steps to ensure the uptake of actual mergers, would be beneficial.

(28) In the first half of 2024, Croatia had the third highest electricity price in the EU for business/industrial consumers. This continues to hold back the cost competitiveness of Croatian companies. Despite the record increase of 397 MW of solar capacity in 2024, the share of solar energy in electricity generation remains low, at less than 6%. Against this background, faster roll-out of new renewable energy capacity – especially solar – and non-fossil flexibility solutions could help reduce price levels. The increased uptake of large-scale renewables, including solar, is hampered by an uncertain regulatory framework as the national energy regulator (HERA) is yet to adopt updated grid connection fees, which creates uncertainty for potential investors and has effectively prevented projects from securing financing. Increased investment in the electricity grid beyond the investments included in the Croatian recovery and resilience plan will be crucial to promote the uptake of renewable energy in Croatia. In the short term, this will require measures to incentivise hybrid storage and renewable energy projects. In 2023, only 24% of household consumers had smart meters installed, which is significantly less than the EU target of 80%. To be able to fully capitalise on the increased uptake of renewable energy, significant funding for the roll-out of smart meters beyond the measures in the recovery and resilience plan as well as dynamic contracts, will be needed to empower consumers and foster demand response. Revising and simplifying administrative procedures for installing renewable energy projects, including in multi-apartment buildings, would help reduce the reliance on fossil fuels. Administrative procedures for setting up energy communities should also be reviewed as the number of registered energy communities remains low.

(29) Energy efficiency measures are necessary to maintain the positive momentum created by the recovery and resilience plan and accelerate progress in: (i) building renovation; (ii) the supply of energy-efficient housing, in particular social housing; and (iii) the replacement of gas and oil boilers with heat pumps and other more efficient and green solutions. Relevant price signals for electrification are also hindered by a tax burden disproportionally skewed towards electricity for both households and industrial consumers. Considering its exposure to climate-related risks and their potential economic impact, Croatia would also benefit from accelerating climate adaptation and water resilience through swift implementation and close monitoring of adaptation and sustainable water management policies, based on nature-based and climate-proof investments in strategic infrastructure.

(30) Road transport is the most used mode of transport in Croatia for both passengers and freight. Reforms and investments under the Croatian recovery and resilience plan – such as modernising railway infrastructure, promoting green transport, and deploying intelligent transport systems – already support these objectives; nevertheless, sustained efforts remain necessary. Modernising the transport infrastructure and the railway rolling stock, increasing the use of public transport and further greening it, putting in place intelligent transport systems, and promoting the uptake of zero-emission vehicles, for example by revising taxation incentives, can greatly contribute to the decarbonisation of the transport sector and reduce the reliance on fossil fuels and energy demand. In 2023, Croatia had the lowest share of renewable fuels in transport in the EU (0.9% vs EU average of 10.8%). Revising rules on blending and mixing of biofuels could encourage the use of alternative fuels. Croatia records sizeable fossil-fuel subsidies without a planned phase-out before 2030. In particular, fossil-fuel subsidies that address neither energy poverty in a targeted way nor genuine energy security concerns, hinder electrification and are not crucial for industrial competitiveness could be considered a phase-out priority. In Croatia, fossil-fuel subsidies such as the ongoing emergency price cap on petroleum products and gas, as well as partial refunds of excise duties for diesel in commercial transport are economically inefficient, perpetuate reliance on fossil fuels and disincentivise electrification and the shift to zero-emission vehicles and other sustainable solutions.

(31) Positive trends in Croatia's labour market continue, though persistent structural and regional challenges weigh on competitiveness and growth potential. Labour and skills shortages are reported across many sectors, while the employment rate remains below the EU average, particularly for vulnerable groups such as older people, low-skilled workers, and persons with disabilities. The disability employment gap has widened considerably, increasing the risk of poverty and social exclusion for disadvantaged groups. Limited participation in adult learning, especially outside the capital region, constrains the development of labour-market-relevant skills and contributes to skills mismatches. Croatia is implementing a series of measures to address labour market needs, some of which supported by the recovery and resilience plan and the European Social Fund Plus. These measures include active labour market policies, upskilling and reskilling programmes, and reforms to better integrate foreign workers into the labour market. However, there is a need to intensify these efforts and improve their effectiveness by more closely targeting vulnerable groups, addressing training gaps, incentivising adult learning participation and improving labour-market-relevant skills, including through high-quality curricula at various levels of education. Advancing the reform of the education system would help achieve higher participation in early childhood education and care and more instruction time in schools, strengthening basic skills and providing a better basis for further education and skills acquisition. Continued efforts are needed to increase the share of qualified teachers of mathematics and physics to improve those skills and participation in science, technology, engineering and mathematics (STEM) studies.

(32) Despite some progress and significant policy efforts, Croatia continues to face significant social challenges. Poverty and income inequality rates are still high, particularly among older people, persons with disabilities and those living in rural areas. In 2023, the risk of poverty or social exclusion remained high in Croatia. The impact of social transfers (excluding pensions) on poverty reduction is among the weakest in the EU, and the adequacy and coverage of minimum income schemes and unemployment benefits are still limited. Pensions are comparatively low, and, at the same time, the system's sustainability is challenged by demographic pressures and a history of early retirement. The availability of long-term care is limited, with yet insufficient access to home care and community-based care, placing disproportionate care burdens on informal carers, especially women, which means they are less likely to work or look for a job. Ensuring effective and coordinated implementation of the 2030 National Housing Policy Plan would contribute to making housing more affordable. Addressing these challenges would also contribute to supporting upward social convergence, in line with the Commission services' second-stage country analysis of the Social Convergence Framework[17].

[17] Commission Staff Working Document: Second-stage country analysis on social convergence in line with the Social Convergence Framework (SCF), SWD(2025) 95 final.

(33) The uneven distribution of doctors is a major barrier to accessing healthcare services in remote/rural regions. Addressing shortages of workers requires initiatives to increase the number of healthcare workers, and improve training, recruitment and retention, paying particular attention to geographical disparities. The share of the population using online health services is one of the lowest in the EU. Although the recovery and resilience plan supports telemedicine services in remote and island areas, a concerted effort is needed to promote equal access to healthcare services, especially to primary and outpatient/ambulatory care.

(34) In view of the close interlinkages between the economies of euro-area Member States and their collective contribution to the functioning of the economic and monetary union, in 2025, the Council recommended that the euro-area Member States take action, including through their recovery and resilience plans, to implement the 2025 Recommendation on the economic policy of the euro area. For Croatia, recommendations (2), (3), (4) and (5) help implement the first euro-area recommendation on competitiveness, while recommendations (4) and (5) help implement the second euro-area recommendation on resilience, and recommendation (1) helps implement the third euro-area recommendation on macroeconomic and financial stability set out in the 2025 Recommendation.

HEREBY RECOMMENDS that Croatia take action in 2025 and 2026 to:

1. Reinforce overall defence and security spending and readiness while ensuring debt sustainability in line with the European Council conclusions of 6 March 2025. Adhere to the maximum growth rates of net expenditure recommended by the Council on 21 January 2025, while making use of the allowance under the national escape clause for higher defence expenditure.

2. In view of the applicable deadlines for the timely completion of reforms and investments under Regulation (EU) 2021/241, accelerate the implementation of the recovery and resilience plan, including the REPowerEU chapter. Accelerate the implementation of cohesion policy programmes (ERDF, JTF, ESF+, CF), building, where appropriate, on the opportunities offered by the mid-term review. Make optimal use of EU instruments, including the opportunities provided by the InvestEU programme and the Strategic Technologies for Europe Platform, to improve competitiveness.

3. Address the fragmentation of public research institutes and universities by setting goals in performance agreements that promote consolidation, collaboration, and, where relevant, mergers, backed by financial incentives to boost scientific output and public return on R&D investment. Foster investments in research and innovation. Boost access to diverse sources of financing for businesses and promote capital markets by further facilitating the participation of retail investors, including in the bond market, addressing barriers to listing, and strengthening corporate governance to improve the attractiveness of the stock market. Further simplify regulation, improve regulatory tools and reduce administrative burden through digitalisation to facilitate business creation and expansion. Reinforce the capacity and efficiency of the public administration at the local level by merging functions and/or municipalities.

4. Address high electricity prices for businesses by accelerating deployment and grid connection of renewable energy projects. Further upgrade electricity transmission and distribution grids, invest in electricity storage and advance the roll-out of smart meters. Streamline permitting, including for energy communities, and simplify the procedures for installing solar photovoltaic facilities in multi-apartment buildings. Accelerate the implementation of energy efficiency measures, especially in residential buildings and reduce the dependence on fossil fuels in the heating sector, including by accelerating the use of efficient and green solutions, such as heat pumps. Reduce reliance on fossil fuels and energy demand in the transport sector by promoting sustainable urban transport, rail and the electrification of road transport, including by reviewing targeted taxation incentives. Take concrete steps to phase out fossil fuel subsidies in particular in the transport sector. Address the recent decline in the share of renewables in transport by revising the rules on biofuels.

5. Reduce labour and skills shortages by removing obstacles to labour force participation, ensuring stronger educational foundations at every level, in particular for basic and science, technology, engineering and mathematics (STEM) skills, strengthening upskilling and reskilling, better targeting active labour market policies to vulnerable groups, and strengthening efforts to attract, develop and retain talent. Strengthen labour market policies and their coordination with social services. Reduce poverty and income inequality by increasing the adequacy of social benefits, including pensions, while maintaining fiscal sustainability. Improve access to formal home- and community-based long-term care. Promote balanced geographical distribution of health workers and facilities, investments in e-health, and closer cooperation between all levels of public administration on health policy.

Done at Brussels,

For the Council
The President