

University of Economics, Prague

International Business - Central European Business Realities



Entry Strategy for the European Union-Republic of Croatia

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Declaration:

I hereby declare that I am the sole author of the thesis entitled “Strategy for the European Union: Republic of Croatia “. I duly marked out all quotations. The used literature and sources are stated in the attached list of references.

In Prague, August 20, 2012

Hana Merdita

Annotation

Key Words: Republic of Croatia, European Union, Stabilisation and Association Process, Convergence Criteria, Croatian National Bank, Accession Negotiations.

More than twenty years after the independence declaration, Republic of Croatia is facing the second biggest step in its history- entry to the European Union. European Union, the world's trade leader, has recognized Croatia as a reliable partner in the future affairs. Croatia shall become a 28th member of the integration on July 1st, 2013.

Croatia has experienced many obstacles on the path to the European Union, trying to align its system with the EU's comprehensive legislation. The aim of this thesis is therefore to provide an extensive analysis of the Croatian path to the European Union and to apply the solutions on the further development not only of Croatia but also the remaining candidate countries of the European Union.

Anotace

Klíčová slova: Chorvatská republika, Evropská unie, Proces stabilizace a přidružení, Konvergenční kritéria, Chorvatská národní banka, přístupová jednání.

Více než dvacet let po prohlášení nezávislosti se Chorvatsko chystá na druhý největší krok ve své historii-vstup do Evropské unie. Evropská unie, nejvýznamnější hráč ve světovém obchodě, uznala Chorvatsko jako spolehlivého partnera pro budoucí členství. Chorvatsko se tak 1. července 2013 stane členským státem Evropské unie.

Chorvatsko pocítilo mnohé překážky na cestě k Evropské unii, ve snaze sladit svůj systém s obsažnou legislativou EU. Cílem této práce je tedy kompletně analyzovat chorvatskou cestu k Evropské Unii a na této bázi formulovat doporučení pro další rozvojový proces nejen Chorvatska, ale i zbývajících kandidátských zemí Evropské Unie.

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Introduction

The aim of this master thesis is to provide an appropriate analysis of the economic challenges that the Republic of Croatia confronted, confront and will confront within its attempts to fairly and successfully access the European Union. Since the creation of the European Union, Republic of Croatia was still defending its status of a newly independent country. It took some time for Croatia to consolidate the system and to defend its status of a strong economy in the region as well as to become competitive enough against the EU member-states to start the accession period. Croatian path towards the European Union was pretty long and the obstacles that were on the country's way were mainly rising from its economic vulnerability.

The goal of the thesis is to give an explanation for the following questions: What are the main characteristics of the European Union and eurozone? How sustainable was Croatian economy during the whole process of accession to the European Union? Which goals did the Republic of Croatia reach in its attempts to fulfil the EU requirements? Which are the prospects for the Croatian further development after the entry to the European Union?

We will, hereby, after brief introduction to its crucial institutions, examine the Accession Criteria of the European Union that should be fulfilled in a country's attempts to succeed after submission of the application for membership. As for the one of the western Balkan countries, accession requirements for the Republic of Croatia have been much more comprehensive than it was for any other western and/or northern European country. We will put an emphasis on the Copenhagen Criteria and explain the importance of each of its conditions in order to understand the sense of Copenhagen Criteria as a whole.

The short description of eurozone and its core functions that follow will prepare *us* for understanding the convergence criteria and the later discussions on euro and the eurozone.

After brief description and explanation of each criterion, we will be introduced to the current position of Republic of Croatia against European Union and see the general characteristics of Croatian first moves on the way to the EU. Here, we will peek into the challenges that were presented to Croatia and which had to be fulfilled. We will also explain the meaning of

Stabilisation and Association Process and its importance for those countries that cannot immediately skip to the negotiations process with European Union. Hereafter, we will be able to imagine not only political but also economic Croatian position against the other countries that applied for the EU membership in that period. The last part of the chapter will show us the outcomes of the referendum right after the country became an acceding country.

Additionally, it is important to explain deeply the current flow of the economic and financial affairs of Republic of Croatia with a strong emphasis on those affairs which could be affected or entrench the regulatory system of the European Union. This chapter will include mainly theoretical and numerical characteristics as well as the explanation of the causes that preceded them. This all will help us to understand the advantages of the entry to the European Union for such country. In addition, we will analyze in detail the performances in economic sphere that the Republic of Croatia had in the past years, as well as its current and future, expected performances in its attempts to access the European Union. This part is very comprehensive, and the emphasis is put mainly on the amount in which the country is indebted, on consumption trends and the interventions of the Croatian National Bank the crisis periods.

In the next chapter we will get to the beginning of the negotiations process between Croatia and European Union. We will go through each of the 35 chapters that were opened between these two entities. Some of the chapters were closed quite early and some of them were more time consuming for Croatia in attempts to harmonize the system according to European Union's requirements. Time consuming were especially those chapters related to judiciary and those which required raising competitiveness of the institutions. We will stress four chapters as these were related to the financial alignments with the EU legislation. Hereby we will stay linked to our previous analysis. I have chosen four chapters in which Croatian National Bank was authorized for implementation of some reforms. We will, hereby, compare all the challenges of various changes in Croatia's system given by the authorities in the domestic scene. This will give us the view of all the data which will explain the readers the reasons why the Republic of Croatia is valuable for the future of European Union and, in contrary, which are potential threats after Croatia's entry to the European Union.

The following chapter will be dedicated to the projections of the Croatia for the near future, those expected by the country itself under the concrete programme of the European

Commission. This will be followed by the explanation of the situations in which the projections could or could not be possible.

In the last chapter we will provide an argumentative feedback on the whole process of the Croatian accession process which will summarize the most crucial issues that Croatia had and has to align with the European Union. We will thereafter provide the analysis with useful suggestions for the Country to become more competitive in the future and give the appropriate recommendations for the remaining candidate countries to establish properly working economic environments.

1. European Union and Accession Criteria

1.1. Basic Information on the European Union

This subchapter is reserved for creating better understanding of the term European Union, its institutions, bodies and the policies that will be mentioned through our further examinations. In order to define the term European Union, we will use its official webpage europa.eu. According to this source, European Union is “a unique economic and political partnership between 27 European countries”.¹

The beginnings of European integration laid in the idea of Jean Monnet to set the control over Ruhr area. Thereupon, German and French production of coal and steel were put under the common authority and the idea was introduced to public by French minister of foreign affairs Robert Schuman on May 9, 1950.² The date had been taken as the “Europe Day” and is has been celebrated on yearly basis. This event preceded the next formation, European Coal and Steel Community. On April 28, 1951, Belgium, France, Italy, Luxembourg, Netherlands and Germany signed a Treaty of Paris, wherewith Monnet becoming its Senior Commissioner. The Treaties of Rome were signed by the same ECSC countries on March 25, 1957 (came into force on January 1, 1958) and represented formations of European Economic Community and European Atomic Energy Community. First, EEC was established with an aim to set the new rules for forming the new common market for the free flows of goods, services and capital. EUROATOM was the base for the new investigations in the area of atomic energy in civil purposes. In 1973, here came the formation of the stronger policy of foreign affairs by the enlargement of the customs union by Denmark, Ireland and Great Britain.³ Eighth decade of 20th century brought another enlargement, whereby Greece, Portugal and Spain joined European Community and in 1986, a Single European Treaty was signed, hereby opening the

¹ Basic Information, European Union, http://europa.eu/about-eu/basic-information/index_en.htm, accessed on 05/08/2012

² “European Foreign Policy”, <http://istfak.files.wordpress.com/2009/10/hill-european-foreign-policy.pdf>, page 12, accessed on 28/08/2012

³ Article on history of European integrations, “Povijest europskih integracija”, Croatian Ministry of Foreign and European Affairs, 2011, <http://www.mvep.hr/ei/default.asp?jezik=&ru=505&sid=>, accessed on 01/06/2012

new opportunities for establishing even stronger form of the single market and enriching the laws by the new management domains. In 1993, the Maastricht Treaty was enforced and the term European Union became an official title for the former European Community. Union's competence remained on three pillars:

“The "first pillar": the Community dimension, comprising the arrangements set out in the EC, ECSC and EUROATOM Treaties, i.e. Union citizenship, Community policies, Economic and Monetary Union, etc.;

The "second pillar": the common foreign and security policy, which comes under Title V of the EU Treaty;

The "third pillar": police and judicial cooperation in criminal matters, which comes under Title VI of the EU Treaty. “⁴

Fourth enlargement occurred in 90ies of 20th century when Austria, Finland and Sweden entered the European Union.⁵ The largest wave occurred in 2004, when European Union was enriched by Cyprian, Czech, Estonian, Latvian, Lithuanian, Hungarian, Maltese, Polish, Slovakian, Slovenian, Bulgarian and Romanian membership on January 1st, 2007.

The three pillars which were mentioned above were on December 1st 2009 replaced by another power degrees, with some changes added to the voting system by the Lisbon Treaty. From this point, fewer decisions are made unanimously, whereas more of them are made by qualified majority.

1.2. Institutions of European Union

In order to understand the issues that will be mentioned in our further discussion, it will be very important to understand how European Union is organized. Its institutional framework is based on seven institutions which will be mentioned in our further discussion.

⁴ European Convention Glossary, <http://european-convention.eu.int/glossary.asp?lang=EN&content=P>, accessed on 14/08/2012

⁵ “European Economy ». European Commission Occasional Papers, http://ec.europa.eu/economy_finance/publications/publication7548_en.pdf, page 10, accessed on 28/08/2012

European Parliament: This institution is personification of the interests of European Union. It can be composed of maximal number of 751 members (Lisbon Treaty) representing each member country of the European Union.⁶ Each member country can be represented by minimal number of 6 representatives and maximal number of 96. European Parliament is empowered to adopt the laws of European Union along with the Council of the European Union. The institution is also authorized to control activities of the European Commission. Communication in the Parliament flows in 23 languages, with the head office of European Parliament in Strasbourg, whereas the Secretariat General of the Commission is situated in Luxembourg while the political groups mostly gather in Brussels.

European Council: European Council represents a forum where presidents or governments of the member countries organize so called summits three to four times per year since 1947. These summits are made in form of two-day forums, enabling representatives to discuss their opinions and decisions. It is also important to know that European Council is focused on the problems of the Union on the general basis, and not on sectoral. Through Intergovernmental Conferences (organized months-long conferences), European Council decides upon the important changes in the structure of the European Union.

Council of the European Union (Council or Council of Ministers): In order to fairly represent the interests of each member country, Council gathers 27 ministers of which each is a representative of his own country. The Council is done at many levels which are responsible for different sets of issues and is made of 10 different formations. In order to keep decisions above the national levels and to help the Council to schedule meetings and to set the topics that will be discussed, here can be found the additional structures such as COREPER (from French *Comité des représentants permanents*, the body that gathers ambassadors of the member-states). Council solves six basic tasks: adoption of laws; coordination of broad economic policy; conclusions of the agreements between the European Union and other countries or international organizations; defining and implementation of the common and foreign security affairs; approval of the budget; coordination of the cooperation between the national courts and the police forces in criminal issues. Another very important role within the Council is called

⁶ Laurent Pech, „The Institutional Development of the EU post-Lisbon: A case of plus ça change...?“, <http://www.ucd.ie/t4cms/11-5%20Pech.pdf>, page 21, accessed on 28/08/2012

Council Presidency. The Presidency is performed each six months (rotation system) by one of the member states. The state can be hereby empowered to conduct the activities of the Council and to prove its ability to retain the good relations among the member states.

European Commission: This institution exists to uphold the interests of the European Union independently from the interests of individual member states. Official languages of the institution are French, English and German and its seat is in Brussels. European Commission proposes, creates drafts and represents the new proposals for law. Along with European Court of Auditors, Commission navigates and monitors the budget of European Union. The other task of the European Commission is the protection of the contracts. The institution consists of 27 commissaries (one per member state) whose mandates take five years.⁷

The Court of Justice of the European Union: In order to uniform the interpretations and implementations of the laws within the Union, the Court of Justice of the European Union was established with its seat in Luxembourg. Such as European Commission, this institution is composed of 27 members (judges) from the individual member states, but for the 6-years' mandates. These judges are assisted by eight advocates in charge of giving their own opinions on the matters submitted. Court is the highly empowered institution that monitors both, national and supranational law regulations and their implementations, operating exclusively under the laws of the European Union, not on the national level.

European Central Bank: The main financial institution that operates as a Euro steering wheel and controls the price stability among the European Union' member countries was established in 1998 and is situated in Frankfurt, Germany.⁸

⁷ "The European Commission Overview", World Law Direct, 2011, <http://www.worldlawdirect.com/article/456/european-commission-overview.html>, accessed on 28/08/2012

⁸ "United Nations-Natur Cons", <http://naturecons.weebly.com/united-nations.html>, accessed on 28/08/2012

1.3. European Union Accession Criteria

Legally, every country that belongs to the European territory can decide and apply for becoming a member of European Union. Still, each of these countries is obliged to respect certain rules and fulfil all the necessary conditions to reach this goal. It is all about the applicant country and its capability to adjust its system to the requirements of the European Union. First step for the applicant country is to request the Council. The role of the European Commission is to provide an opinion on the applying country, but it is the Council that will give the permission for accepting the application.⁹ The basic rules that have to be fulfilled before country will be allowed to start negotiating with all the other member countries are so called Copenhagen criteria (1993, Copenhagen) and are separated into four parts. These parts, as quoted and described on the official web site of European Commission, are following:

“Political criteria: stability of institutions guaranteeing democracy, the rule of law and respect for human rights, including the rights of minorities;

Economic criteria: a functioning market economy and the capacity to cope with competition and market forces;

The capacity to take on the obligations of membership, including adherence to political, economic and monetary objectives;

Creation of the conditions for integration through the adjustment of administrative and institutional structures guaranteeing effective implementation of the acquis “ (set by Madrid European Council in 1995).¹⁰

⁹ Enlargement Policy, European Commission, http://ec.europa.eu/enlargement/the-policy/conditions-for-enlargement/index_en.htm, accessed on 19/06/2012

¹⁰ Accession Criteria, European Commission, http://ec.europa.eu/enlargement/glossary/terms/accesion-criteria_en.htm, accessed on 19/06/2012

1.4. Historical Overview of Eurozone and Its Functions

The turning point for the whole Europe, as well as for the rest of the world was when 11 member states of the EU (Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain) on January 1. On January 1, 2002, notes and coins of euro were introduced and national currencies entered the eurozone system. Additional countries that have joined European Monetary Union since 1999 were Greece in 2001, Slovenia in 2007, Cyprus and Malta in 2008 and Slovakia in 2009. Agreement on the currency usage was also signed by five other territories: Mayotte, Monaco, San Marino, Saint Pierre & Miquelon and the Vatican and there are also some that have unilaterally adopted the euro as the official currency: Andorra, Kosovo, Montenegro, Saint Barthélemy, Saint Martin and the British Sovereign Bases on Cyprus. Independent European Central Bank is the official institution for the governance of the euro system in help of President and full-time executive, whereas the bank's council is responsible for the interest rates' decision-making processes. These decisions are being regularly sent to the executives of the central banks of all the member states of eurozone for the further usage.

The introduction of euro as a currency came as a result of ratification of the Treaty of Maastricht in the early 1990s, whereas the idea of establishing such common currency started much earlier, at European Summit in Den Haag and the Werner Report (Luxembourg's Prime Minister Pierre Werner) for economic and monetary union and the framework for the European Monetary System.¹¹ However, the circumstances regarding the problems of the US dollar convertibility and the boom in the oil prices meant the beginning of the plan stagnation.¹² Instead of setting the new common currency, these circumstances made the countries intervene by moderating the exchange rates among their currencies and to set the European Monetary Cooperation Fund.

In order to stimulate the economic activities of the European countries, it was necessary to launch the program for stabilization of the intensely floating exchange rates. This led to the establishment of the European Monetary System in 1979. In February 1986, the Single

¹¹ "From the Werner Report to Euro", Prof. Dr. Hans Tietmeyer, 2003, http://www.bcl.lu/fr/bcl/pierre_werner/discours_tietmeyer.pdf, accessed on 28/08/2012

¹² EMU, A Historical Documentation, European Commission, http://ec.europa.eu/economy_finance/emu_history/history/part_a_2_a.htm, accessed on 19/06/2012

European Act enriched the EEC Treaty with some important points on the further functioning of the European Economic System and stimulated the creation of the European Currency Unit. The discussion culminated at the Hannover Summit in June 1988, where the President of the Commission Jacques Delors was suggested to start with the measurements for the final economic and monetary union' creation. This boosted the creation of institutional framework for proper institutional arrangement of the future monetary union. Delors Committee finally provided a draft of the report on EMU in the European Community in April 1989, where the three stages of creation economic and monetary union were suggested.¹³ The idea was fully adopted and the first stage started on July 1 1990 with some modifications which were adopted at the end of the same year. After the Intergovernmental Conference on EMU launching, there was another one, discussing the idea of political union. The result of these two conferences was a 2-day Maastricht Summit in December 1991, where the name "European Union" was given to the political form of union. "Economic and Monetary Union" was set up on the basis of EEC Treaty. Maastricht Treaty comprised these two unions and was ratified in April 1992. The Treaty has been in force since November 1, 1993.¹⁴

If a certain country wants to enter the European Monetary Union, there are criteria that have to be fulfilled as a warranty of monetary stability. These criteria are called Convergence Criteria, also known as Maastricht Criteria and these are the following:

"The amount of money owed by a government - known as the budget deficit, has to be below 3% of Gross Domestic Product (GDP) - the total output of the economy.

The total amount of money owed by a government, known as the public debt, has to be less than 60% of GDP. The public debt is the cumulative total of each year's budget deficit.

Countries should have an inflation rate within 1.5% of the three EU countries with the lowest rate. This was supposed to push down inflation rates and lead to more stable prices.

Long-term interest rates must be within 2% of the three lowest interest rates in EU.

¹³ "A single European Currency: Why the United Kingdom Must Say 'No'", The Bruges Group, 1996, <http://www.brugesgroup.com/mediacentre/index.live?article=113>, accessed on 28/08/2013

¹⁴ "Political Aspects of European Monetary Integration After World War II", Horst Ungerer, 1995, http://aei.pitt.edu/7026/1/ungerer_horst.pdf, accessed on 28/08/2012

Exchange rates must be kept within "normal" fluctuation margins of Europe's exchange-rate mechanism.”¹⁵

Usually, countries are motivated to enter monetary union because of the securities and the benefits that such union provides. Sovereign countries are attempting to establish as stable economies as possible and to stimulate their economic growth. In EU, medium of evaluation of the stability of countries' exchange-rate mechanism in comparison with the others is ERM II. If a country wants to change its national currency into euro, it has to pass this evaluation. Regarding the macroeconomic stabilization' processes of the countries, there are documents which are provided in order to help the new member-countries to correctly guide their markets and to adjust their employment policies. These are, for instance, “Broad Economic Policy Guidelines”, “Growth Pact” and “Stability and Growth Pact”. Stability and Growth Pact is mainly oriented on binding the countries to coordinate their budgetary policies and to reach surpluses or very low deficits on the accounts.¹⁶

2. Republic of Croatia on the Way to the European Union

Currently, there is one acceding country and five candidate countries for the European Union. Republic of Croatia is, nowadays, the only country with status of the acceding country to the European Union. Candidate countries are Montenegro; Republic of Island; the Former Yugoslav Republic of Macedonia; Republic of Serbia and Republic of Turkey.¹⁷

The relationship between Republic of Croatia and the EU rises from the beginning of 1992 when Croatia was internationally recognized as the independent state. The relationship between the two entities was reinforced in 1999 which lead to the entering the European Union's Stabilisation and Association Process.

¹⁵ Convergence Criteria, BBC News, 2001, http://news.bbc.co.uk/2/hi/in_depth/europe/euro-glossary/1216651.stm, accessed on 07/08/2012

¹⁶ “Alternatives to the Stability and Growth Pact-proposals for a new fiscal policy regime”, 2004, page 7, http://www.arbeiterkammer.at/bilder/d24/Endfassung_engl_Vers1.pdf, accessed on 28/08/2012

¹⁷ Kristin Archick, “European Union Enlargement”, <http://www.fas.org/sgp/crs/row/RS21344.pdf>, page 5, accessed on 28/08/2012

This process started by signing the Stabilisation and Association Agreement, hereby opening the first serious commitment of the Republic of Croatia towards other members of the EU, besides the commitment of fulfilling the Copenhagen Criteria. This represented the new era for the country. The Agreement was signed on the 29th of October, 2001 in Luxembourg. From this point, Republic of Croatia changed its status to the potential candidate for the EU. As a guarantee about Croatian devotion to implementation of all the chapters of Agreement, Croatia has to transmit monthly reports about the outcomes of its implementations and is obliged to such transmissions by the Implementation Plan of the Agreement.¹⁸ Since the SA Agreement was signed, Croatia has been strictly called to support and to maintain the regional cooperation with its neighboring countries in the South East Europe.

Next that the Republic of Croatia undertook was an application for the European Union' membership on 21st February 2003¹⁹. After filling a questionnaire made of 4560 questions, European Commission brought positive opinion on Croatian request for EU membership application therefore offering the beginning of the accession negotiations. The confirmation of Croatia as a candidate country brought a special attention to Croatian cooperation with the International Criminal Tribunal for the former Yugoslavia which is inevitable for maintaining good relations in the region and broader. Accession negotiations were therefore opened on 3rd October 2005, right after the confirmation that Croatia was fully cooperating with the ICTY.²⁰

Seventeen days after the "Screening stage" was initialized, meaning that the 35 chapters of the accession negotiations had to be fulfilled. The process was completed on June 30, 2011. Six months later, on 6th December, admission of Republic of Croatia was resolved and after just three days the Accession Treaty was signed. According to Croatian Constitution, the country is obliged to organize referendum, enabling its citizens to participate in the decision-making process on every important issue that the country is facing.

¹⁸ CROATIAN ACCESSION TO THE EUROPEAN UNION, Economic and legal challenges, Katarina Ott, <http://bib.irb.hr/datoteka/158516.EU-eng.pdf>, accessed on 10/08/2012

¹⁹ Croatia on the Way to the European Union, Croatian Parliament, <http://www.sabor.hr/Default.aspx?sec=385>, accessed on 19/06/2012

²⁰ "The Enlargement of the Union", European Parliament, http://www.europarl.europa.eu/ftu/pdf/en/FTU_6.3.1.pdf, accessed on 10/08/2012

Referendum on EU Accession took place on 22nd January with the following turnout:

“Total voters: 1 960 231 (43, 51%)

Valid ballot papers: 1 948 498 (99, 44%)

In favor of European Union: 1 299 008 (66, 27%)

Against the European Union: 649 490 (33, 13%)”²¹

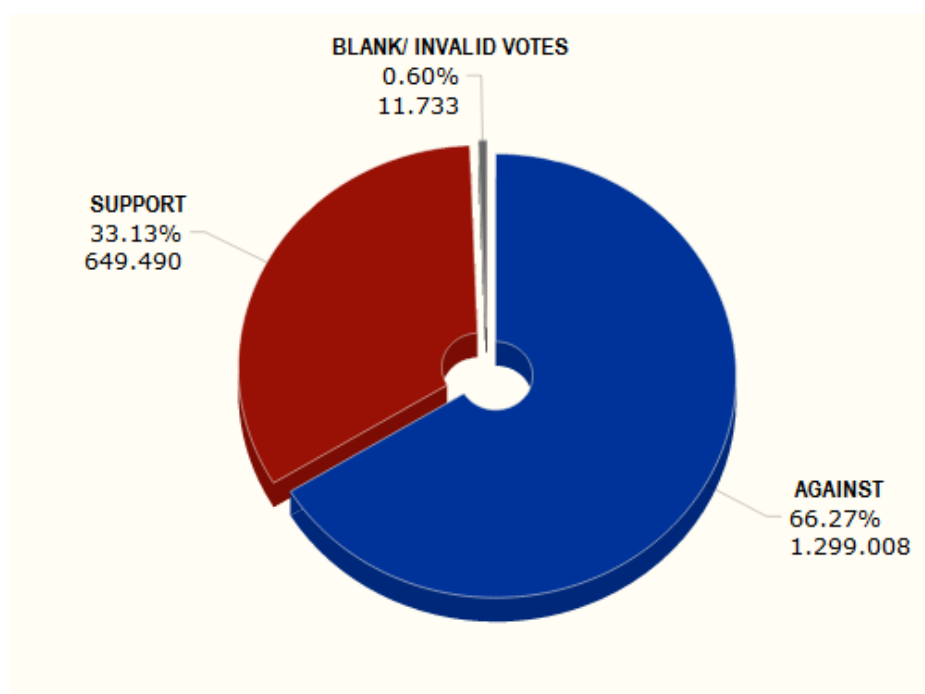


Figure 1: Structure of Votes on Croatian Referendum for Joining European Union

Source: Elections²², 2012

²¹ Elections, 2012, <http://www.izbori.hr/2012Referendum/rezultati/rezultati.html>, accessed on 20/06/2012

²² Elections 2012, <http://www.izbori.hr/2012Referendum/rezultati/rezultati.html>, accessed on 20/06/2012

Despite the huge diversity of opinions throughout media, where some authors is afraid of too high level of euro scepticism in the Republic of Croatia, the results of referendum represent a great triumph for the majority of Croatian politicians. Republic of Croatia is becoming a member of European Union on July 1, 2013.

2.1. European Union's Stabilisation and Association Process

Our question is which sectors were the most vulnerable and how did Republic of Croatia handle the whole process of stabilisation of its institutions in various sectors (with an emphasis on banking sector) in order to engage in proper cooperation with other member-countries of the EU. In this section we will first of all examine some issues related to trade and transport provisions between European Union and Republic of Croatia. These issues were noted in Interim Agreement officially valid since 1st March 2002.²³ This agreement is consisted of 53 articles which are, in fact, particular articles taken from Stabilisation and Association Agreement.²⁴ For Croatia the Agreement meant a connection to the Stabilisation and Association Agreement. It was tailored to stimulate the following changes in the then EU-Croatia relations:

- “– establishment of an association between the Community and its Member States, of the one part, and the Republic of Croatia, of the other, six years after entry into force of the agreement;*
- establishment of a formal framework for political dialogue with the Republic of Croatia, at both bilateral and regional level;*
- enhanced regional cooperation;*

²³ **CHALLENGES OF CROATIA AND EU INTEGRATION: is the fast track approach possible?** *International Issues Journal*, Bratislava, March 2005, Visnja Samardzija, Ph.D' Institute for International Relations, Zagreb, Croatia

²⁴ EUROPEAN COMMUNITY – CROATIA INTERIM AGREEMENT, <http://www.worldtradelaw.net/fta/agreements/eccrofta.pdf>, page 15, accessed on 05/08/2012

– *promotion of economic and commercial ties, with a view to establishing a free-trade area covering goods and services, following a transitional period of six years after entry into force of the agreement;*

– *regulation of the free movement of workers, freedom of establishment, supply of services, current payments and movement of capital;*

commitment by the Republic of Croatia progressively to harmonise its legislation with that of the European Community, notably in key areas of the internal market;

– *establishment of wide-ranging relations covering every field of Community interest and including cooperation in the field of justice and home affairs;*

– *complete liberalisation of road transit traffic across the Republic of Croatia and the Community as a whole and development of the accompanying infrastructure, within a specific protocol on land transport which takes into account the lack of any prior agreement on transport;*

– *formal granting of Community financial and technical assistance to the Republic of Croatia to help implement certain aspects of the agreement;*

– *establishment of a specific institutional framework in the form of a Stabilisation and Association Council to supervise implementation of the agreement, a Stabilisation and Association Committee and a Stabilisation and Association Parliamentary Committee.”²⁵*

Hereby, the first step towards the whole stabilization process was launched. Interim agreement was valid until February 1, 2005, when the Stabilisation and Association Agreement came into force. The Interim Agreement regulated mainly the issues based on trade and transportation between Croatia and EU. There was also an important note, in political preamble, regarding Croatian approximation to the European Union regardless of the level in which the other countries of the region cooperated with the EU. Since the Stabilisation and

²⁵ Quotation, STABILISATION AND ASSOCIATION AGREEMENT BETWEEN EUROPEAN UNION AND REPUBLIC OF CROATIA and INTERIM AGREEMENT, 2001, http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/er/13344.en1.html, accessed on 05/08/2012

Association Agreement was signed, Republic of Croatia obtained status of a potential candidate for the EU membership and it was supposed to start harmonize its legal framework as well as the other aspects step by step and to start stress good relations with other countries in the region as well as the relations with the EU member states.

This was all covered with the Stability Pact and its Memorandum for Free Trade Liberalisation and Facilitation that was signed in 2002, along with the other SAP countries. Croatian government was thus encouraged to take bigger efforts to establish the ground for major economic changes on the local basis and under their leadership. Stabilisation and Association agreement is a preferential agreement, assembled for an undefined period. The most time consuming part was the one concerning the harmonisation of trade regulations, regarding the liberalisation of industrial and agricultural products from the European Union.

2.2. Croatia and Convergence Criteria: After Euro Introduction

We are here interested in the extent in which Republic of Croatia was prepared for such union as the European Monetary Union at the moment and several years after the euro was introduced.

In January 2002, Croatia started with using consumer price index as a methodology for calculating its average annual rate of inflation, which did not match with the methodology used in EU.²⁶ Croatia still could not use such methodology due to the fact that there were no consumption of the nonresidents and the consumption of the institutional households (until 2007, when the reform started). This is why there was a problem in analogy of inflation rates in Croatia and the one in the European Union. Still, if we take data from Croatian Bureau of Statistics, we will notice that the institution was using, such as Eurostat, Harmonized Indices of Consumer Price. Another step Croatia should take to fulfil the next criterion. It would have to

²⁶ "EU Criteria with Special Emphasis on the Economic Convergence Criteria; Where is Croatia?" Michael Faulend, Davor Lončarek, Ivana Curavić and Ana Šabić, <http://www.hnb.hr/publikac/pregledi/p-019.pdf>, accessed on 31/05/2012

exchange GFS 2001, prepared by International Monetary Fund for ESA 95 methodology to calculate the budget deficit accordingly.

As regards the exchange rate stability, we can say that HRK/EUR fluctuations are stable. However, it has to be decided after the accession, according to the fluctuation range in the near past and actual fluctuation range, whether it has been narrow enough and whether the capital transactions are liberalized to fulfil the criterion. In further discussion, we will describe the latest 2012 HRK/EUR relationship and the process of liberalization. Since the introduction of euro, Croatia has had most of its long-term arrangements issued in euro or in other currencies so it is not easy to estimate real readiness of Croatia to meet the long-term interest rate criterion.

3. Economic and Financial Affairs in the Republic of Croatia

This subchapter will show us how the economic area had been built during the whole process of system' harmonisation and which were the consequences of all the actions taken. In order to fully understand economic and financial affairs and its complexity during the period of Croatian accession to the European Union, we must take into account that Croatian economy is very young and, anyhow, its development was largely affected by the happenings during the Homeland War in 1990ies. We will therefore describe its development step by step in order to better understand the complexity of all the actions that were about to be taken to correctly harmonize of the system anent the accession to the European Union.

Croatia was a part of the Socialist Federal Republic of Yugoslavia until June 25, 1991, when the independence was declared, by both Croatia and Slovenia. This was the official beginning of military operations in the area which brought general disasters for the directly affected areas as for the rest of the region. The agony lasted until the Dayton Agreement in December 1995 when the Bosnian territory was distributed between Croatia, Serbia and Bosnia and Herzegovina.

Period between 1990 and 1993 brought Croatia the hardest economic crisis, where the high inflation of 35 % led to almost 30% drop in GDP.²⁷ It called for huge amounts of money and efforts to supplement the damages that Croatian nation was facing as well as to protect the territory from further disasters. In October 1993, Kuna, Croatian currency was introduced along with pronouncing Croatian National Bank as a central banking institution. It was followed by the liberalisation of interest rates.²⁸

Despite the huge challenges, the government brought the countries exchange rate level to the enviably stable position in 1994-1998 periods due to the broad fiscal consolidation policies. Attractiveness of the nominal exchange rate ceiling which made 3,7 HRK/DEM (after appreciation from 4,444 HRK/DEM) and building of new banks with convenient deposit rates gave a momentum for huge capital inflows. However, this position turned to be just temporary. Due to enlarged role of the state in economy it was hard to obtain the positive trends among the other countries, where private sectors were in flourishing, liberalised phase. In this period, in which Croatia was facing huge expenses to botch the losses that occurred during the war-period, and the banks struggled for success within the large competition, the country was getting less competitive towards the others and there was a new recipe for success needed. However, instead of encouraging domestic economy with rise in production, Croatian spending was directed mainly to the consumption of goods and services, of which the majority came from foreign countries.²⁹

Even though Republic of Croatia was ranked by World Bank stats quite positively in terms of income in 1998 (upper-middle income), the rearrangements of the system were inevitable to maintain such reputation. In that time, government was relatively positive towards the idea of encouraging the economic and financial system with clearly determined objectives with respect of questions relating the realisation of fully functional free market economy. Nevertheless,

²⁷ Croatia Economic Vulnerability and Welfare Study, World Bank, 2001, http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2001/05/11/000094946_0104270504592/Rendered/PDF/multi0page.pdf, accessed on 07/08/2012

²⁸ Transmission Mechanism of Monetary Policy in Croatia, Maroje Lang and Ivo Krznar, 2004, <http://www.hnb.hr/dub-konf/10-konferencija-radovi/lang-krznar.pdf>, accessed on 31/05/2012

²⁹ Croatia Economic Vulnerability and Welfare Study, World Bank, 2001, http://www-wds.worldbank.org/servlet/WDSContentServer/WDSP/IB/2001/05/11/000094946_0104270504592/Rendered/PDF/multi0page.pdf, accessed on 07/08/2012

there was an obvious lack of vision related to the costs of such realisation. Moreover, these objectives seemed not to encourage the citizens to engage into the program and it didn't meet clear response of Croatian citizens who were still getting used to the new structure of the state in general, using all the benefits provided by huge number of banks, to fulfil their personal needs. On the crossroad from 1998 to 1999, this led to the negative stream for smaller or medium-sized banks which started to lose their competitiveness and couldn't persist any longer. The situation brought CNB to react by setting the new equilibrium for HRK/EUR. Even though Croatia lost many foreign investors during the war period, due to positive trends and more or less stable financial environment in the post-war 1990s, the situation in 2000 was quite promising. Let's see how Croatian monetary policy was structured during the early 2000s and which its main characteristics were. It is crucial to understand which changes evolved under the new circumstances, such as an existence of euro. We will use data from Croatian National Bank's reports as a trustworthy source for overview.

In 2000, Government debt repayment made considerable changes in economic liquidity and started to manage the reserves' rate throughout the year. In 2001, there was another shift-liberalization of Law on Foreign Exchange, which led to currency movement due to the impetus of the companies and, especially, banks to treasure foreign currencies. It was a clear call for CNB to start selling foreign currencies. CNB reacted immediately, but the actions were not strong enough to cover the consequences of accumulation of foreign currencies in the commercial banks.³⁰

3.1. Republic of Croatia: Readiness for the European Monetary Union between 1995-2001.³¹

Within the six-year period, we can perceive considerable advantages that Croatia possessed against the other CEE countries:

³⁰ Transmission Mechanism of Monetary Policy in Croatia, Maroje Lang and Ivo Krznar, 2004, <http://www.hnb.hr/dub-konf/10-konferencija-radovi/lang-krznar.pdf>, accessed on 31/05/2012

³¹ "Makroekonomski aspekti pridruživanja Hrvatske Europskoj Uniji", Dubravko Mihaljek, <http://www.ijf.hr/Eu/mihaljek.pdf>, accessed on 07/08/2012

Exchange Rate Stability: There were notable growths in exchange rates in the CEE countries in 1995-2001. For instance, Czech Republic and Hungary counted 25% growth, almost 50% in Poland and 20% in Slovakia, while in Croatia just 4% was recorded.³²

Positive trend towards export activities and in balance of current payments: Between 2000 and 2001, there was 9% growth in exports of goods and services and 3.1% deficit in balance of current payments in 2001, while in Czech Republic, Poland and Slovakia this deficit counted 5 and 6% in the same year.

Direct Foreign Investment: In the same period, Croatia was very attractive for foreign direct investments and it was in the growing phase. In that period, only Czech Republic had considerably higher tendency of FDI to grow.

High Foreign-Exchange Reserves: At the end of 2001 CNB held more than five months coverage of imports of goods and services.

However, there were some very unfavourable aspects in Croatian economy against the other CEE countries that could not guarantee much success:

Total Foreign Debt (%GDP): At the end of 2001, total foreign debt of Republic of Croatia counted even 56% of its GDP, which was more than in any other CEE country except Hungary (65% of GDP) with tendency to grow.³³

Ability to Repay the Foreign Debt: Country's ability for repayment, where for the repayment of accrued interest rates and for the principal of the foreign debt it takes 20% of income made by the exports of goods and services gives very negative forecasts for the future projects.

Interest Rate on Public Bonds: Interest rate scale is still very high. It makes 190 of percent points, which were 70-90 points more than in Czech Republic, Hungary and Slovakia.³⁴

³² "Makroekonomski aspekti pridruživanja Hrvatske Europskoj Uniji", Dubravko Mihaljek, <http://www.ijf.hr/Eu/mihaljek.pdf>, accessed on 07/08/2012

³³ "Makroekonomski aspekti pridruživanja Hrvatske Europskoj Uniji", Dubravko Mihaljek, page 48, <http://www.ijf.hr/Eu/mihaljek.pdf>, accessed on 07/08/2012

3.2. Further Development of the Financial Sector in Croatia

Liberalization on Law of Foreign Exchange in 2001 was just a first step towards variety of new changes that occurred in 2002. As the banks were severely distressed by foreign exchange deposits, they started to call their parent banks for interventions in order to stay competitive on the Croatian market. This boosted huge debentures where the CNB's measures against growth in foreign indebtedness were the biggest threats for banks. Therefore, some of them started either to get onto debt at their parent banks or transposing some of their businesses to the related firms.³⁵ The year was also characterized by huge amounts of investments in infrastructure, where the combination of personal spending and highways' constructions contributed greatly to the growth of the real annual GDP rate that reached 4.7% in the period between 2002 and 2005. Highways' construction stimulated great amounts of capital investments on the public account as well as on the private sector accounts.

In 2003, this was all accompanied by an absolute liberalization of the long-term capital flow and the liberalization of short-term capital was announced. Transactions' processes in Croatia were therefore encouraged, whereas European Union was facing deceleration in economic activities which additionally brought deceleration in interest rates and capital and bonds contribution rate. This situation was extremely attractive for foreign investors. Regarding the bank accounts' indebtedness, they were in very bad condition in 2003. It reached even critical 32% at annual level and banks started to place most of their foreign assets to the population that invested mostly in credit purchase of automobiles. Subsequently, result was a fast growth in imports which jumped from 17.2% in 2002 to 32.5% in 2003.

³⁴ Macroeconomic Aspects of Croatian Accession to the European Union, Dubravko Mihaljek, <http://www.ijf.hr/Eu/mihaljek.pdf>, accessed on 07/08/2012

³⁵ Analysis of Croatian Foreign Debt, Croatian National Bank, <http://www.hnb.hr/publikac/ostale-publikacije/h-analiza-inozemne-zaduzenosti-rh.pdf>, accessed on 07/08/2012

Events in 2003 worked mostly in favour of domestic banks, where the huge credit activities of banks and struggling for the market shares led to the markup of foreign obligations.³⁶ As the current cash flow within the country was already quite exhausted by consumption and other expenses, the country could not rely on repayment of its capital requirements through the current sources of its capital returns, it kept on relying on the foreign resources even in 2004. However, thanks to the new strategy for reduction of budget deficit brought positive results.

In 2005, foreign public debt was reduced to the minimum. In comparison with 2003, where the increase in foreign debt in public sector made 31.3% and in 2004 foreign debt increased for 13.6%, in 2005 the increment in public sector was 7.3%. Still, it is important to take into account that these positive changes in public sector reflected on the increment of foreign debt in other sectors, especially banking. Therefore, in this period the greatest increment in foreign debt comes mainly from the private sector. In the following figure, we will describe proportion of short-term foreign debt in the total foreign debt, according to the original maturity during the whole period between 1998 and 2005:

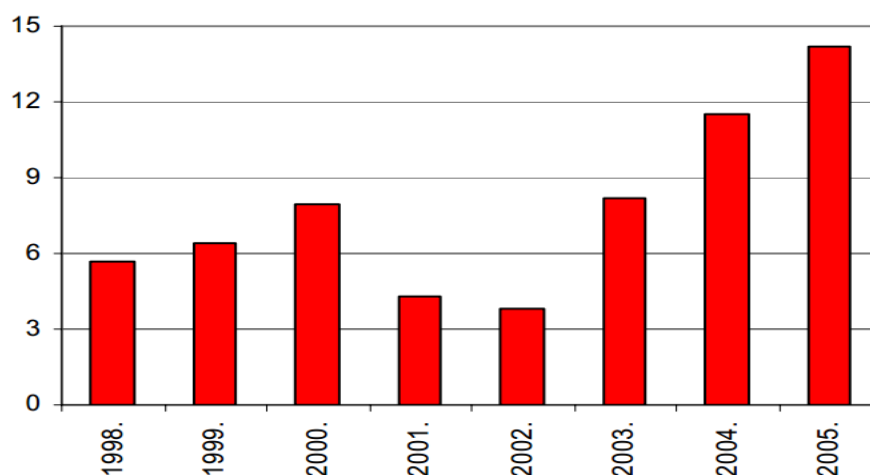


Figure 2: Proportion of the Short-term Foreign Debt in the Total Foreign Debt (1998-2005); Source: Croatian National Bank, 2006.

In our figure, we can notice significant drop in the short-term foreign debt during the 2001 which occurred mainly as a result of the drop in the total short-term public debt. From 2003 on,

³⁶ Analysis of Croatian Foreign Debt, Croatian National Bank, <http://www.hnb.hr/publikac/ostale-publikacije/h-analiza-inozemne-zaduzenosti-rh.pdf>, accessed on 31/05/2012

there is a noticeable boom in short-term foreign debt, as a result of the increase in banks' short-term obligations.

It is also important to understand the currency structure of the Croatian foreign debt at the end of 2005. The structure is viewed in the following figure:

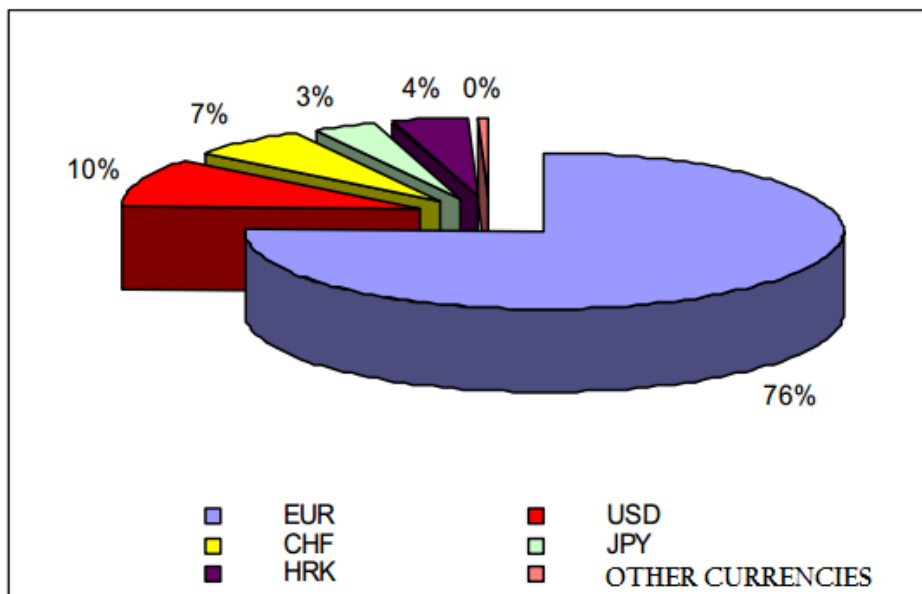


Figure 3: Structure of Croatian Foreign Debt at the end of 2005;

Source: Croatian National Bank, 2006.

In Figure 3, we can notice clear predominance of foreign currencies in the Croatian foreign debt at the end of 2005. Mainly it is structured by euro, followed by dollar and only 4% is made of Croatian kuna. Huge amount of euro debt comes from the situations where the banks are calling their parenting banks for interventions.

If we compare Croatia with the other CEE countries in the given period, we will see that Croatia is the most indebted country. Taken into account the amount of foreign debt in GDP, Croatia takes first place in the indebtedness. While in the other countries proportion of foreign debt was almost 52% in 2004, Croatia had the average of even 80.2% in the same year.

Romania and Czech Republic found themselves in the best position against the others, while in Bulgaria and Slovakia the annual alteration remained unchanged.³⁷ In Croatia, here was the highest growth rate in foreign debt between 2002 and 2004, counting even 19.2%, while in the other countries the average was 8.6%.

Since 2005, Croatian government launched a broad program to raise an investment spirit within Croatian society and to attract foreign investors into the Republic. However, the country was already exhausted by the previous matters where indebtedness was getting intolerable. Lower proportion of public debt in GDP between 2005 and 2008 was going hand in hand with investment encouragement. Within this period, there was a positive drop in the foreign component of public debt from 44,7% (2005) to 30,2% (2008). Nominal value of public debt raised in 2009, due to the overall financial crisis. Congruently, GDP also dropped from 34.159,0 HRK to 333.063,0 HRK. In the Table 2 in appendix, we will see the structure of the public debt between 2005 and 2010.

Unfortunately, Croatia was seriously affected by the global economic crisis in 2009. Budget incomes were decreasing, GDP was getting lower and the nominal value of the public debt increased. For the first time after five years, the state started with issuing bonds on the foreign markets. At the end of September 2010, the public debt jumped to 133,9 billion of HRK, which made even 40,4% of the then estimated GDP. During the year, gross amount of the foreign debt raised by 0,9 billion of euro, due to the depreciation against the US dollar and Swiss franc. Hereby, the total gross amount of the foreign debt in December 2010 made even 46,4 billion of euro.³⁸ In the following figure we will see the currency structure of the foreign debt in 2010:

³⁷ Analysis of the Croatian Foreign Debt, Croatian National Bank, <http://www.hnb.hr/publikac/ostale-publikacije/h-analiza-inozemne-zaduzenosti-rh.pdf>, accessed on 31/05/2012

³⁸ Croatian National Bank Annual Report on 2010., 2011, <http://www.hnb.hr/publikac/godisnje/2010/h-god-2010.pdf>, accessed on 31/05/2012

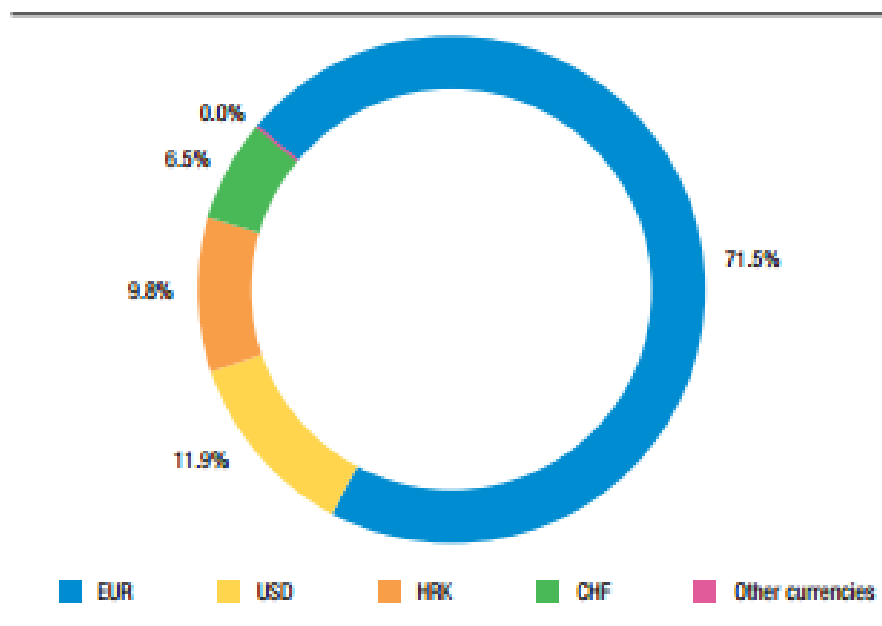


Figure 4: Currency Structure of the Croatian External Debt in 2010.

Source: Croatian National Bank, 2011.

<http://www.hnb.hr/publikac/godisnje/2010/h-god-2010.pdf> , 31/05/2012

During 2010, Croatia was marked up by increasing unemployment rate, due to financial crisis. This negative trend started at the end of 2008 and presents a serious problem within the society. In 2008, even 56 051 people lost their jobs, while in 2010 this number grew to unbelievable 66 330 of the people that lost their employment.

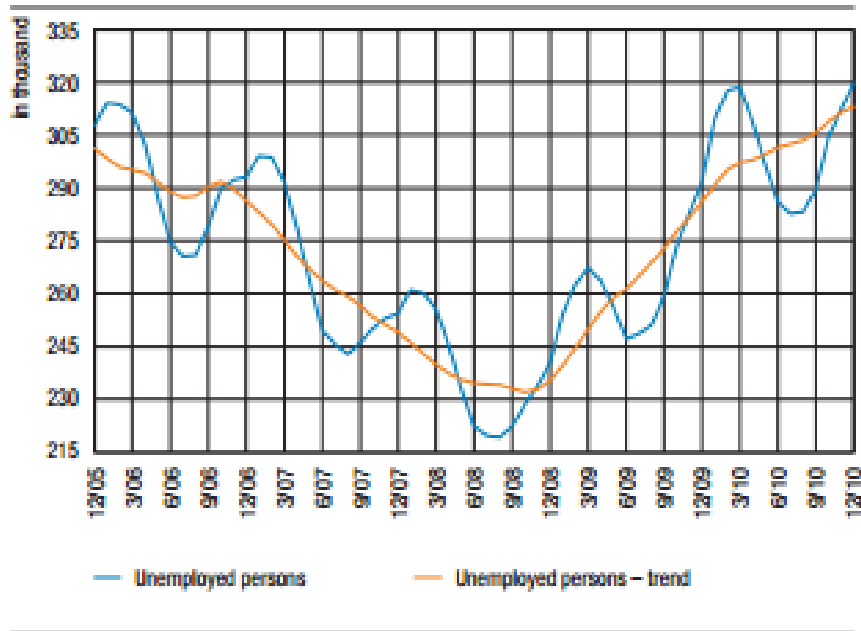


Figure 5: Unemployed Persons Registered in the Croatian Employment Service (2010)

Source: Croatian Employment Service, 2011.

Even though there was a smoother deviation in the number of unemployed during 2009, at the end of 2010, the number of registered unemployed persons increased to 319 845 of the unemployed persons.³⁹ According to this, an average unemployment rate in 2010 was 18,6%.

We will now focus on the recent past years (2011. and a part of 2012.) and take a closer look at the Croatia's economic and financial performance, in order to have a clearer overview of the approximate conditions under which Croatia will join European Union.

In 2011, we could not notice considerable changes in GDP. In comparison with the other SEE countries, Republic of Croatia found itself in the most unfavourable condition, especially in terms of exports in previous years. In the second and fourth quarters of 2011, due to touristic

³⁹ Croatian Employment Service, <http://www.hzz.hr/>, accessed on 14/08/2012

season, Croatian engagement had experienced smaller revival. However, this position did not have long standing effects. Increment in exports of goods and services and changeover in storage contributed largely to the revival. During the year, there was a noticeable growth in the service industry. Still, the manufactures and construction engineering had negative trend. Regarding the unemployment rate, even though it was very unexpected, we will notice smooth recovery by the end of 2011. During the year, there was a visible drop in the number of employed persons in private sector, whereas in the public sector this number increased. In 2011, number of registered unemployed persons at the Croatian Employment Service was 315 438, which was 17,8% of the total amount of labour force.

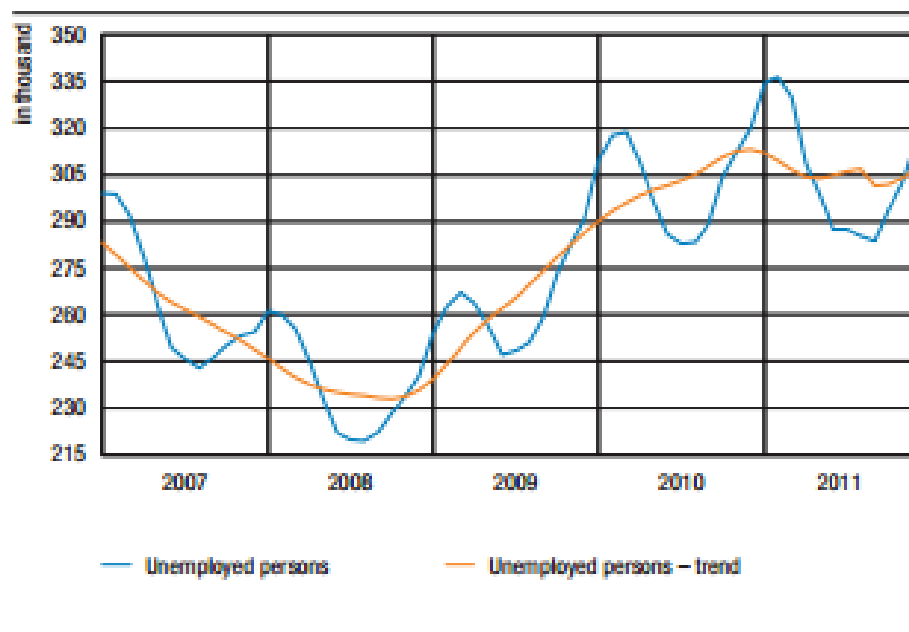


Figure 6: Unemployed Persons Registered in the Croatian Employment Service (2011)

Source: Croatian Employment Service, 2012

Inflation rate increased especially because of the prices of imported products and an increase in prices of energy-generating products and raw materials on the international level. Therefore, the increase in the inflation rate of consumer prices in 2011 was even 2,3% (in comparison with 2010,

when the annual inflation rate of consumer prices was 1,1%. This increase was sensible especially in foodstuff. The following graph displays the monthly rates of the core inflation on annual basis. Here, the agricultural products nor those products that are regulated on the administrative level.

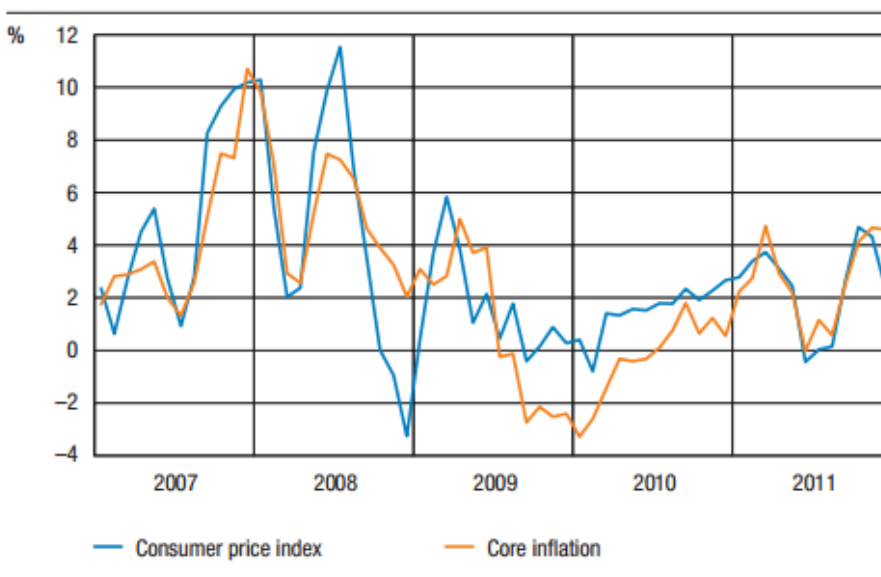


Figure 7: Consumer Price Index and Core Inflation

Sources: Croatian Bureau of Statistics, 2012. and Croatian National Bank, 2012.

In 2011, Croatian National Bank kept on supporting the stable nominal exchange rate between kuna and euro as the basic condition to maintain the financial stability within the country and to control the level of prices.⁴⁰ The two exchange rate interventions were undertaken by National Bank to smoothen the situation of the decrease in capital inflow and discharging towards foreign creditors. By the end of the year, the Bank also increased the rate of compulsory reserve from 13% to 14%, which led to the depreciation in exchange rate of 2,0% against the one in the previous year. The banking sector was facing fewer requests from the companies and the population's deposits were rare.

⁴⁰ RBA Annual Report, 2011, <http://www.rba.hr/web/pdf/annual-report/rba-annual-report-2011-en.pdf>, 2011, page 5, accessed on 15/08/2012

In the financial system good liquidity dominated, so the overnight interest rates were mostly under 1%. Active, as well as the passive banks' interest rates had diminishing tendency until the end of the year, when the crisis on the international level had its impact on the domestic system. Regarding the risk perception, the situation in Croatian banking system was worse than the previous year. In spite of the credit burden that banks had to deal with, they managed to maintain stable level of earnings. Good touristic trend in Croatia had positive effects on the current account of the balance of payments. Increasing general government debt to HRK 156,0 billion, in other words to 45,7% of GDP due to the new borrowings to cover public unfavourable public finances in 2011.⁴¹ In 2011, gross external debt was 0,7% lower than the previous year. It made HRK 45, 7 bn., especially because of some private enterprises that turned parts of their debts into their equity for EUR 1,5 billion. In the following figure we will demonstrate the currency structure of the debt, where we could see considerable change in the euro portion of the debt:

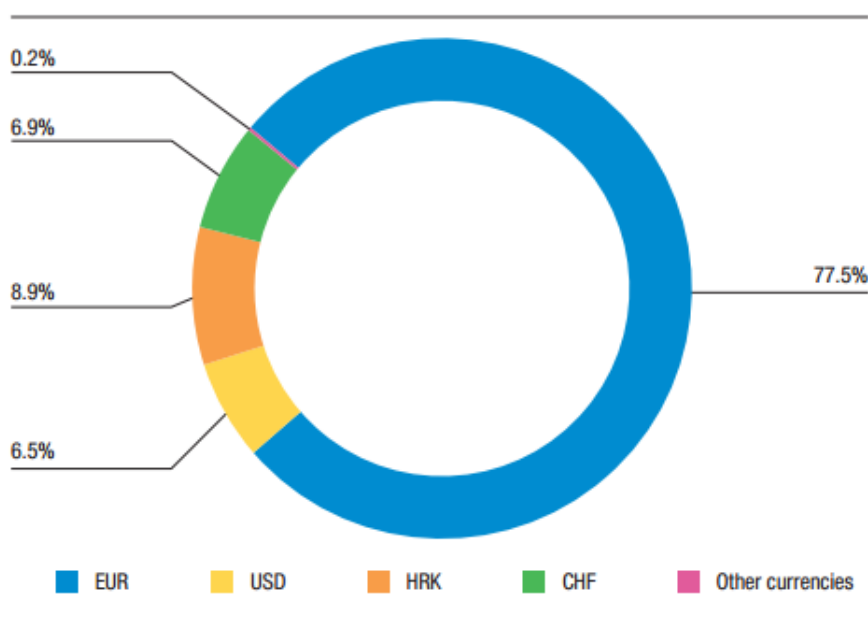


Figure 8: Currency Structure of the Croatian External Debt in 2011.

Source: Croatian National Bank, 2011, <http://www.hnb.hr/publikac/godisnje/2010/h-god-2010.pdf>, 31/05/2012

⁴¹ CNB's Annual Report, 2012, <http://www.hnb.hr/publikac/godisnje/2011/h-god-2011.pdf>, accessed on 31/05/2012

In 2012, Republic of Croatia still has managed floating regime which fluctuates in accordance with the situation on the foreign exchange market which, on the other hand, is a response to the foreign exchange of goods and services, indebtedness, foreign investments, or the tourists' inflow. Still, Croatian National Bank can intervene whenever it predicts too high inflation rate, which can mainly rise from overflowing transactions in euro. As the ongoing critical economic situation in the eurozone is still quite instable in 2012, and Croatia has its major trading partners in the zone, there are no good perspectives for the future exports.⁴² Moreover, the country will have to make considerable changes in the economic policy and save the perception among the foreign players.

According to Croatian Bureau of Statistics, in March, 2012 dangerous 20% unemployment rate was recorded. At the same time, growing consumer price index can be assigned to the growing VAT rate which was a part of new economic reforms in the beginning of 2012. In March 2012, a warning sign came from Fitch, global credit rating agency. Fitch confirmed BBB- rating for Croatia, with negative outlook. This is the lowest investment level.⁴³ Fitch's note was that despite the fact that Croatia worked hard and made took some positive steps, further structural reforms and fiscal consolidation is inevitable. Moody's long-term rating for Croatia is Baa3 with negative outlook.⁴⁴ This is newly updated record in May 2012, while the previous record from Moody's was also Baa3, but with stable outlook in April 2009.⁴⁵ Standard & Poor's rating for the Republic of Croatia is BBB- with negative outlook (2010), changed from BBB with negative outlook in 2009.⁴⁶ In the table below, we will demonstrate the latest midpoint exchange rates' trend.

⁴² CNB's Annual Report on Financial Stability, <http://www.hnb.hr/publikac/financijska%20stabilnost/h-fs-9-2012.pdf>, accessed on 31/05/2012

⁴³ Fitch Rating, 2012: <http://www.fitchratings.com/gws/en/esp/issr/80442240>, accessed on 08/08/2012

⁴⁴ Moody's: http://www.moody.com/research/Moodys-changes-outlook-on-Croatias-Baa3-rating-to-negative-from-PR_247199, accessed on 08/08/2012

⁴⁵ http://www.hnb.hr/rejting_rh/e-moodys.pdf, accessed on 08/08/2012

⁴⁶ S&P Rating : <http://www.standardandpoors.com/ratings/sovereigns/ratings-list/en/us/>, accessed on 08/08/2012

Table 2: Midpoint Exchange Rate by Croatian National Bank for July, 2012.

Source: Croatian National Bank, 2012

Midpoint Exchange Rates of the Croatian National Bank for July 2012 updated 2 August 2012		
	Average	End of period
EUR/HRK	7.494496	7.518303
CHF/HRK	6.241017	6.262643
GBP/HRK	9.489191	9.614198
USD/HRK	6.089386	6.124391

4. Croatia's Accession Criteria fulfilling and its Advancement

Croatia became an official applicant of the European Union on February 21, 2003 after the receipt of European Commission's "positive opinion". On October 4, 2005, the negotiations between two sides began.⁴⁷ In this chapter, we will closely analyze the whole process of how the Republic of Croatia adjusted its national law to all the 35 chapters of the European Union's *acquis*.

We will describe briefly each chapter separately and concentrate on four chapters and the detailed advancement of their fulfilling. These chapters are Chapter 4: Free Movement of Capital; Chapter 9: Financial Services; Chapter 17: Economic and Monetary Policy, and Chapter 32: Financial Control. While analysing Croatian macroeconomic aspects we could have noticed that in many crises' situations Croatian National Bank showed up as the reliable institution for healing these occasions. In order to stay in line with our previous discussion, the criterion for choosing particular negotiations' chapters was choosing those chapters in which Croatian National Bank was authorized to participate in decision-making processes in attempts to align Croatian system with the EU's legislation.

Chapter 1: Free Movement of Goods

The first chapter of the negotiations with the European Union arises from the idea that the products should be traded freely within the borders of the EU. There are two regulatory frameworks that are applicable for particular sectors.⁴⁸ The old approach where the specifications for the products are very detailed and the new approach with the general requirements for the products. There is also a proof of the sufficient capacity for providing regular reports on the trade restrictions needed. Croatia has proven all its capacities and the chapter was provisionally closed on April 19, 2010.

Chapter 2: Freedom of Movement for Workers

A country is responsible to ensuring that all the workers will be free in choosing in which member-country to work including the same treatment as the domestic workers are provided,

⁴⁷ "Negotiations EU-Croatia", <http://www.delhrv.ec.europa.eu/?lang=hr&content=66>, accessed on 10/08/2012

⁴⁸ Free Movement of Goods, Croatian Ministry of Foreign and European Affairs, <http://www.mvep.hr/ei/default.asp?gl=200111020000009>, accessed on 31/05/2012

along with the same work conditions and tax and social reliefs. Expatriate workers with their families must be given the coordinated national social insurances. The chapter was provisionally closed on October 2, 2009.

Chapter 3: Right of Establishment and Freedom to Provide Services

The member-states must adjust their national legislations in the way that no legal or national persons of the European Union will be prevented from establishing or providing the services on the territory of the European Union. The *acquis* also provides a regulatory framework for mutual recognition of qualifications and diplomas as well as the mutual recognition of particular occupations.⁴⁹ This chapter was closed on February 21, 2009.

Chapter 4: Free Movement of Capital

This chapter includes all the questions regarding investments, investment funds, credits, deposits, insurance and asset transfers. Negotiations on free movement of capital were opened on the Intergovernmental Conference on October 2, 2009. This chapter is consisted of three basic areas of interests: free movement of capital, money transfers' services, and suppression of money laundering and terrorism financing.⁵⁰ Basic articles on free movement of capital are regulated in the Stabilisation and Association Agreement on which Republic of Croatia based its process of liberalization in movement of capital and eliminated the limits that existed in the movement of capital as well as in exchange of real estate.⁵¹

The main institutions that were authorized to implement the adjustment of the legislation to the *acquis* of the European Union were Croatian Ministry of Finance, Croatian Ministry of Justice and Croatian National Bank.

⁴⁹ "Hrvatska i Europska unija; Prednosti i izazovi članstva", Sanja Tišma; Višnja Samardžija; Krešimir Jurlin, Institut za međunarodne odnose-IMO; Zagreb, 2012, http://delhrv.ec.europa.eu/files/file/articles-hrvatska_i_eu_prednosti_izazovi-1326211380.pdf, accessed on 23/08/2012

⁵⁰ Report on the commitments' fulfillment (Chapter 4), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/04_sloboda_kretanja_kapitala/poglavlje_04_izvjesce_o_ispunjenju_obveza/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/04_sloboda_kretanja_kapitala/poglavlje_04_izvjesce_o_ispunjenju_obveza/(view_online)/1), accessed on 13/08/2012

⁵¹ Negotiation Process' Standpoints (Chapter 4), [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/04_sloboda_kretanja_kapitala/poglavlje_04/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/04_sloboda_kretanja_kapitala/poglavlje_04/(view_online)/1), accessed on 13/08/2012

In order to adjust the Foreign Exchange Operations Act to the *acquis communautaire*, the Act was modified three times due to the global financial crisis so that some restrictions were kept even after 2006. However, since January 1, 2010, all the capital transactions have been liberalized except two restrictions that are supposed to be eliminated within a given period. Regarding the transactions with stocks, these were also regulated in modifications from 2006. Regulations on investing in foreign stocks have modified as well as on shares of stocks in foreign investment fund. Moreover, stock transactions were liberalized in such way that there are no transactions that would be different for residents or nonresidents left. According to Foreign Exchange Operations Act, banks were not obliged to pay their clients those tuitions of assets from abroad nor the foreign approved loan amounts that were not registered in Croatian National Bank. This act has also been removed. Residents can freely get onto debts based on short or long-term financial credits and can freely accept obligations from nonresidents if the maturity is more than three months. The liberalization of granting the short-term credits to nonresidents was delayed two times and has been valid since July 1st, 2010 in order to avoid the risks of a part of liquidity from the banking sector and possible depreciation threats in the period of financial crisis. The same happened with the act on deposit operations. Even though liberalization of these operations was supposed to come about much earlier, they were delayed for January 1st, 2011.

Since January 1st, 2011, the citizens not only of the Republic of Croatia but also those from the European Union have been free to operate with capital transactions or to do businesses through foreign financial institutions. Since then also the greater transparency of financial institutions has been provided.

There was also questionable act on portage of cash, checks and materialized in and out of the country. This question was solved by absolute liberalization and since January 1st, 2010, all these can be brought in and out of the country, regardless of currency as well as amount, as long as the directives on suppression of money laundering are respected. At the same time, cash payments and tuitions can also be freely committed among residents and non-residents within the European Union's borders under the same conditions. Removal of preferential access of the public institutions into the financial institutions (such as voluntary or compulsory pension-funds, saving-credit cooperatives) by adjustment of several directives was another step towards completing the negotiations' chapter. The removal should be done on the date of Croatian

Accession to the European Union. Moreover, public institutions lost the access to the Fund of Croatian Homeland War' Defenders And their Family Members.

Next liberalization was the one regarding the treatment of institutional investors in investing into domestic and foreign assets. Such liberalization brought the right to authorized persons to freely invest into foreign securities. Croatia is about to bring into force the alliterations in the directives on privatization of INA-Croatian oil industry and the privatization of Croatian Telecommunications with the day of Croatian Accession to the European Union. On February 23rd, 2010, after the directives on the privatization of Croatian Electrical Utility were removed, all the special rights that the state had on this entity were cancelled. Since the day of Croatian Accession to the European Union, the housing saver in Croatia does not have to be a Croatian citizen.

The next criterion for successful closure of the chapter relates to the questions connected to the acquisitions of real estate on the Croatian ground.⁵² Since 2006, many reforms were conducted in order to simplify the process of acquisition of the real estate and of getting the ownership rights for noncitizens of the Republic of Croatia. Since February 1st, 2009, the citizens of the European Union have been treated in the same way as Croatian citizens in the process of the acquisitions of properties. These regulations have some exceptions, as stated in the Stabilisation and Association Agreement. These are the right on acquisition of the real estate on an agricultural land and on the areas protected by Environmental Protection Act.⁵³

Regulations of EC related to the cross-border payments in Community that says that the differences in charges for cross-border and national payments in euro should be eliminated,⁵⁴ are still not a part of Croatian legislation but will be implemented as soon as Croatia enters the European Union.

⁵² Croatia - 2005 Progress Report - {COM(2005) 561 final} {COM(2005) 556 final} /* SEC/2005/1424 */ , 2005, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52005SC1424:EN:NOT>, accessed on 28/08/2012

⁵³ Stabilisation and Association Agreement, http://www.mvep.hr/ei/download/2002/07/05/SSP_cjeloviti_tekst1.pdf, accessed on 31/05/2012

⁵⁴ „Crossborder Payments in Euro“, European Commission http://ec.europa.eu/internal_market/payments/crossborder/index_en.htm, accessed on 31/05/2012

The third criterion necessary for closure of the chapter relates to the suppression of money laundering and financing of terrorism. Republic of Croatia supplies the reports on three-month basis. Alterations in Croatian directives have authorized Financial Inspectorate to take over the role of a supervisory body in this field. According to the act from July 15, 2008, that regulates validation the Convention of Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime and Financing of Terrorism, puts up Ministry of the interior, Police Directorate, Crime Investigation Police Department, Department for Economic Criminality and Corruption and State Attorney's Office of the Republic of Croatia are defined as the central body for the international cooperation and legal aid for this Convention. Moreover, a system of extended confiscation of the property from those persons condemned for organized crimes or corruptive actions was established. Meaningful step in suppression of corruptive activities was also an act on personal identification numbers so the possessions can be better controlled. Within the criterion, some of the other directives were regulated and/or modified, such as acts that regulate credit institutions, police affairs and competences, games of chance, payment transfers, and judicial cooperation in criminal matters with the member-states of the European Union. In the office for money laundering under the Ministry of Finance and in Financial Inspectorate, new departments were added, specialized in particular fields of interests.

MONEYVAL, Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism, the committee that operates under the Council of Europe, brought a report with positive opinion on Croatia's advancement in the system organization in April, 2009.⁵⁵

The chapter was closed on November 5, 2010.

Chapter 5: Public Procurement

Transparency, equal treatment and non-discrimination are the three basic features of the fifth negotiations' chapter. Accomplishment of the item is a basis for economic growth and boosting

⁵⁵ MONEYVAL, Council of Europe, <http://www.coe.int/t/dghl/monitoring/moneyval/>, accessed on 14/08/2012

the market competition. Since February 2005, all the Croatian business providers can be engaged in the public procurement activities.⁵⁶ The chapter was negotiated until June 30, 2010.

Chapter 6: Company Law

This chapter includes all the terms for successful establishment and fairly operating companies, along with the opening opportunity for the companies to easily expand within the European Union's territory without major changes in their actual functioning. Hereby, the companies can easily cooperate and modernize faster.⁵⁷ The chapter was formally closed on October 2, 2009.

Chapter 7: Intellectual Property Law

Protection of intellectual property, such as using copyright and related laws, patents or trademarks is extremely important for maintaining desired reputation on the market and stimulating proper usage of the rights of the others. Republic of Croatia has reached high level of the harmonization with the EU acquis and the chapter was closed on February 19, 2008.

Chapter 8: Competition Policy

Competition policy is a set of rules that regulates conditions under which the companies compete among themselves, hereby creating opportunities to innovate and to set appropriate prices for the consumers. European Commissions' Directorate General for Competition is empowered by Commission to control competitiveness within the cross-border EU's market.

Negotiations on Competition Policy began on June 30, 2010. Croatia had to fulfill four important criteria to provisionally close the chapter. "It had to strengthen its administrative capabilities and to prove satisfactory implementation of market competition. Additionally, Croatia had to complete the juridical harmonization with the acquis. It also had to bring an updated national restructuration program for the steel sector and for particular business plans, accepted by the European Commission, on the steel products, in accordance with Protocol 2. of

⁵⁶ Croatian Standpoints on Negotiations (Chapter 5), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/05_javne_nabave/poglavlje_05/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/05_javne_nabave/poglavlje_05/(view_online)/1), accessed on 13/08/2012

⁵⁷ Company Law, European Commission, http://ec.europa.eu/internal_market/company/index_en.htm, accessed on 19/06/2012

Stabilisation and Association Agreement. Finally, Croatia had to ensure absolute compliance of EU regulations on the state's aid to shipbuilding sector.”⁵⁸

Republic of Croatia took many measures to fulfil requested criteria by setting the appropriate legislative framework for the market competition area and made it opened for all the entrepreneurs on the market, so that they can all enjoy the same terms on the same. In April 2009, adoption of Protection of Market Competition Act supplemented the previous act and made entrepreneurs who try to restrict the competition exposed to larger fines. Restrictions of competitions or abuse of position are penalized by 10% of the total entrepreneur's earnings. Appearance of the leniency programs or amnesty that gives the competent institutions ability to come across cartels in exchange for minimized punishment is also a novelty in the country. Legal security of the entrepreneurs was raised by adoption of the SIEC tests used for the merger control.

Croatian Competition Agency, made of 54 employees, has enlarged competences, meaning that they have a right to make an inquest of apartments or rooms, and to unexpectedly confiscate needed things and documents.

Customization of the Croatian Radiotelevision was carried out in October 2010, by alteration of the Croatian Radiotelevision Act, after which the new agenda was set to boost the competition among the televisions as was as to increase the independence of the public television. It is exactly defined which activities of the television are public and which of them are commercial and works without any political influence or influence of the commercial interest' providers. In order to lower the account deficits, Croatian Radiotelevision took some recovering steps which brought the HRK 105 mil. deficit in 2009 to just HRK 16 mil. deficit in 2010. Important was the decrease in advertising in the prime time as well as the restructuration' program and reduction of the number of employees.⁵⁹

As regards the steel sector, under the National Steel Sector Restructuration Program, two ironworks were privatized between 2007 and 2011. This program was aimed to boost the

⁵⁸ Report on Commitment Fulfillment (Chapter 8), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/08_trz_is_no_natjecanje/poglavlje_08_izvjesce_o_ispunjenju_obveza/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/08_trz_is_no_natjecanje/poglavlje_08_izvjesce_o_ispunjenju_obveza/(view_online)/1), accessed on 13/08/2012

⁵⁹ Agenda, Croatian Radiotelevision, http://www.hrt.hr/fileadmin/video/Program_rada_i_financijski_plan_HRT-a_za_2012.pdf, page 42, accessed on 10/08/2012

profitability of the sector. However, due to the global financial crisis and lower demand under the price fluctuation conditions, the production in both ironworks was decreased.

Steel company Zeljezara Split experienced an absolute suspension in 2009. The company was acquired by Zlomrex S.A. in 2007. Polish company which operates mainly in Poland, Austria and Czech Republic, committed to invest in the company and maintain its business but it did not fulfill the commitment. After 17 short-term loans requested by Croatian Privatization Fund and Zeljezara Split to save the company's business, bankruptcy proceedings were open in March 2011.

Another steel company, CMC Sisak Ltd., was trying hard to sustain on the market. The Company was since 2007 fully owned by US Commercial Metals Company. CMC Sisak brought the Sustainability Plan for 2007-2011, aimed to support launching the technology innovations and to benefit. CMC Sisak inducted better conditions for production and introduced new electrical furnaces. However, due to the financial crisis in 2008, the plan could not be carried out in the expected pace. The company was sold to Italian Danieli Group in April 2012.⁶⁰

Another important concern in Croatian advancement was restructuration and harmonization of Croatian shipbuilding sector so that could sustain on the global market. The goal was to free Croatian citizens from the burdens derived from obstacles in functioning of the sector and reach the sustainability and rent ability of the same.

Restructuration of the shipbuilding sector was launched in 2006, and the shipyards were committed to contribute with at least 40% of share. Horizontal production capacity was supposed to decrease 21%.

Four bids were put in the following shipyards:

- Shipyard Brodosplit BSO: bid by DIV from Samobor, Croatia,
- Shipyard Brodotrogir: bid by Jadranska Ulaganja from Zagreb, Croatia,
- Shipyard Kraljevica: bid by Jadranska Ulaganja from Zagreb, Croatia,

⁶⁰ "CMC sells Sisak steel mill to Danieli Group", <http://daily.tportal.hr/197739/CMC-sells-Sisak-steel-mill-to-Danieli-Group.html>, accessed on 17/08/2012

- Shipyard 3. Maj: bid by Jadranska Ulaganja from Zagreb, Croatia

Potential investors are requested to firstly accept all the restructuring program criteria. It was approved by all the four potential investors that they will implement the restructuring program criteria and contribute to the business activities of mentioned shipyards.

The chapter was closed on June 30, 2011.

Chapter 9: Financial Services

The following negotiations' chapter "Financial Services" includes information on banking sector and other financial services' restructuring in attempts of Croatia to satisfy the European Union's requirements. We can notice from our previous analysis that the banking sector of Croatia had already high level of that concurred the European banking sector at the moment of opening the negotiations. Now, the main objective is to maintain stable financial sector, by effective usage of the opportunity to be a part of the European Financial Supervision. The chapter was opened on the Intergovernmental Conference in June 2007.⁶¹

In the harmonization process, Republic of Croatia had adopted even 15 acts or modifications of the existing acts. The institutions that are responsible for the harmonization of the services with the *acquis* are: Croatian National Bank, Croatian Financial Services Supervisory Agency, Ministry of Finance, State Agency for Deposit Insurance and Bank Rehabilitation, and Central Depository and Clearance Company Inc.

The first study provided by Croatian National Bank that was concerning the capital adequacy rate in order to demonstrate the business practices of the commercial and saving banks showed that the minimal capital adequacy rate was 12%, and capital requirements were increased by 50% which was corresponding to the requirements.

New act was introduced in 2008, on institutions for electronic money and on the supervision over the financial conglomerates. Supervisory system was also fortified by Memoranda of the Croatian National Bank Banque de France, German agency BaFin, financial supervisor of San Marino and with the financial supervisor of Montenegro. At the same time, a setup for the

⁶¹ Report on Commitment Fulfillment (Chapter 9), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/09_financijske_usluge/poglavlje_09_izvjesce_o_ispunjenju_obveza/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/09_financijske_usluge/poglavlje_09_izvjesce_o_ispunjenju_obveza/(view_online)/1), accessed on 13/08/2012

deposit insurance was inducted. Croatian National Bank was responsible for converting savings and loan cooperatives to the credit unions.

Regarding the insurance, Croatia has adopted a new act on obligatory insurance in transport (motor vehicles), hereby preparing the country for entering the Green Card System of the European Union.⁶²

Here, we can also find alteration of the Capital Market Act, which is aimed to bring extended client or investor's protection, establishment of investment trust, directives on effective risk management, and defined capital requirements. Actors on the capital market need to have transparent environment for operation. Only transparency can bring awareness of all the possible risks and consequences of the future arrangements.

Croatian National Bank took measures of stationing of forces within the institution and fortified the supervision of banks. Additionally, workshops provided by CNB were useful instrument to be implemented in the credit institutions.

In the banking sector, also a new IT framework was provided to support better adoption of the changes that occur in the EU legislation.

Regarding HANFA (Croatian Financial Services Supervisory Agency), the agency made the most evident progress of informing the citizens on the novelties through the banks and various institutions, raising their awareness and organized various upgrading trainings and seminars. The agency also published several handbooks for consumers and is continuously informing the public through its bulletin quarterly published on the website.

The chapter was closed on November 27, 2009.

Chapter 10: Information Society and Media

This chapter defines all the conditions for effective functioning of competition policies in the media sphere, emphasizing the interests of the final consumers as well as the providers of the same. Further concern is to inform society on the technological advancement and new

⁶² Croatian Insurance Bureau, <http://www.huo.hr/hrv/povijest-hrvatskog-ureda-za-osiguranje/88/>, accessed on 18/08/2012

opportunities in the information system. A special emphasis is on protection of juvenile from inappropriate contents.⁶³ Information Society and Media was closed on December 19, 2008.

Chapter 11: Agriculture and Rural Development

The main goal of the chapter is to create stable environment for providing a good quality food for accessible prices.⁶⁴ This sector will have the same level of direct payments after the entry to the EU. Still, it is commonly agreed that the contribution of Croatia will keep on decreasing, while the EU funds' contribution will rise. This will lead to the stable market of fair competition among the domestic and foreign producers and will have a tendency to grow and develop. Croatia fulfilled the commitments and the chapter was closed on April 19, 2011.

Chapter 12: Food Safety, Veterinary and Phytosanitary Policy

This is a set of regulations provided to create a secure environment for the consumers among the European Union as well as the environment of insurance and animal and herbs' welfare. European Union dedicated large part of *acquis communautaire* to this chapter, as the member-states agreed to give the authority to the European Union in purpose of setting common standard and better harmonization within a single authority. The chapter was closed on July 27, 2010.

Chapter 13: Fisheries

After the entry to the European Union, Croatia has to have a harmonized legal framework to correctly apply all the requirements related to appropriate usage of fishing morals as well as the coastal and insular fishery management. A year after Croatian entry to the EU, Croatian fishermen and the other fishery organizations will have equal rights to participate in the European Fishery Fund as the others from the Union, meaning they will have better opportunities to modernize and to boost their working habits. Croatia fulfilled the requirements successfully and closed this chapter on June 6, 2011.

⁶³ Croatian Standpoints on Negotiations (Chapter 10), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/10_informacijsko_drus_tvo_i_mediji/poglavlje_10/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/10_informacijsko_drus_tvo_i_mediji/poglavlje_10/(view_online)/1), accessed on 13/08/2012

⁶⁴ Croatian Standpoints on Negotiations (Chapter 11), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/11_poljoprivreda_i_ruralni_razvitak/poglavlje_11/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/11_poljoprivreda_i_ruralni_razvitak/poglavlje_11/(view_online)/1), accessed on 13/08/2012

Chapter 14: Transport Policy

Republic of Croatia has already aligned its transportation sector with the EU standards by introducing some novelties like digital tachograph which is aimed to record the working hours of the drivers that are allowed to drive maximum nine hours a day. This innovation supports fair competition between the drivers.⁶⁵ Transportation policy is useful not only for the drivers but for all the participants in the transportation field. This policy is enriching the level of protection of all the citizens. A comprehensive information system has been installed to control and manage the entire maritime transport of the Croatian Adriatic. Travellers of the air transport are also extra protected since the implementation of the EU standards. They can ask for an accommodation and food as well as the refund in case of the lateness of the airplane or the cancellation of the flight. The chapter was closed on November 5, 2010.

Chapter 15: Energy

In order to maintain growth in energy supply and to effectively fight the emission of greenhouse gases, Croatia adopted Energy Development strategy which will be into force until 2020. It is very important to liberalize energy market to reach competitive environment that will result with affordable prices for all the energy users. Croatia is nowadays raising its capacities for energy storage by supplement of oil stocks. Negotiations on energy between EU and Croatia were closed on November 27, 2009.

Chapter 16: Taxation

EU member-states are allowed to keep their own taxation systems to maintain the good functioning of their internal markets.⁶⁶ Still, they have to adopt the systems against taxation frauds. Here, the member-states communicate through the VAT electronic information system and the Excise Movement Control System and Croatia adopted both systems to stay in line with the others. The chapter was closed on June 30, 2010.

Chapter 17: Economic and Monetary Policy

⁶⁵ Croatian Standpoints on Negotiations (Chapter 14), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/14_prometena_politika/poglavlje_14/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/14_prometena_politika/poglavlje_14/(view_online)/1), accessed on 13/08/2012

⁶⁶ Negotiations EU-CRO: Chapter 16-Taxation, http://www.dnevno.hr/vijesti/svijet/eu/pregovori_rheu_poglavlje_16_porezi/324671.html, accessed on 19/08/2012

The chapter on economic and monetary policy was opened on December 21, 2006, hereby opening various important questions related to the position of the central bank, its integration into the wider system of central banks, euro issues, and, for example, relationship between public sector and financial institutions. Completing this chapter means being prepared for absolute dedication to future sharing of interests leading to the overall common welfare. Each EU member-state is a subject of the Stability and Growth Pact; therefore they are responsible to harmonize their fiscal policies accordingly. New member-states are due to stream towards the ability to join eurozone and until then they are supposed to treat their exchange rates in favor of the general benefit.⁶⁷ Which were the major changes in the implementation of the European Union's requirements?

According to the previous act, Croatian National Bank was responsible to the Croatian Parliament. Nowadays, this institution works autonomously and is only expected to provide reports on the ex-post basis.⁶⁸ However, this independence also includes coverage of all its expenses from its own reserves or the national budget, and no securities can be issued by the state to cover it anymore. The institution is responsible for maintaining stable prices through its activities and the decision-making process is autonomous from the other institutions.

There is another significant change in the system, related to autonomy. State will not have preferred access to the financial institutions such as obligatory and voluntary pension funds nor to the saving-credit cooperatives from the day of the entry to the European Union, hereby raising the level of the institutions' autonomies.

Moreover, supplementation of the legislation secured that the Croatian National Bank will be prepared to join the European System of Central Banks and to adopt euro, which is agreed to become a new national currency as soon as Croatia fulfils all the convergence criteria. Decision on closing the chapter was brought on February 19, 2008.

Chapter 18: Statistics

⁶⁷ Analytical Overview Report, Ministry of Foreign and European Affairs, 2006, <http://www.mvep.hr/custompages/static/hrv/files/pregovori/3/17.pdf>, accessed on 31/05/2012

⁶⁸ Report on the commitments' fulfillment (Chapter 17), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/17_ekonomska_i_monetarna_politika/poglavlje_17_izvjesce_o_ispunjenju_obveza/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/17_ekonomska_i_monetarna_politika/poglavlje_17_izvjesce_o_ispunjenju_obveza/(view_online)/1), accessed on 13/08/2012

Nowadays inhabitants of the democratic countries rely on reliable statistical data in order to reach their business goals. It is important to have good statistical system providing fine assessments not only in the European Union but also on the national basis. Since the chapter was opened, Croatia made considerable moves in modernization and harmonization process. In 2006, new act on employing 461 people in the Croatian Bureau of Statistics was adopted and for 30 new employees in 2007.⁶⁹ The chapter was closed on October 2, 2009.

Chapter 19: Social Policy and Employment

In the European legislation there is a huge concern over providing a unique and fair approach to the social and employment issues. Country interested in joining the European Union is due to ensure safe environment for good implementation of such issues like labour law, health and safety at work, social dialogue, employment policy, anti-discrimination, equal treatment or social protection. Negotiations on social policy and employment were closed on December 21, 2009.

Chapter 20: Enterprise and Industry Policy

Development of competitive environment is one of the major concerns of the European Union. This chapter is occupied with development of the competitive industry under the globalization, demographic changes and the issues of sustainable development.⁷⁰ Entrepreneurs are encouraged to succeed, to modernize and to use and develop new technologies. Opportunities for young people, those with disabilities or women are emphasized within the EU regulations. The chapter between EU and Croatia was closed on July 25, 2008.

Chapter 21: Trans European Networks

This chapter includes all the issues related to Trans European networks in areas of the transport, telecommunications and energy infrastructure, whereas the countries are supported by the European Union through various guidelines on how to develop such networks.⁷¹ The

⁶⁹ Statistics-Chapter 18, Ministry of Foreign and European Affairs, <http://www.mvep.hr/custompages/static/hrv/files/pregovori/4/18.pdf>, accessed on 31/05/2012

⁷⁰ Enterprise and Industry Policy-Chapter 20, <http://www.vecernji.hr/vijesti/20-poduzetnistvo-industrijska-politika-razvoj-konkurentnosti-clanak-301188>, accessed on 05/08/2012

⁷¹ Trans European Networks-Chapter 21, Croatian Ministry of Maritime, Transport and Infrastructure, <http://www.mppi.hr/default.aspx?id=6239>, accessed on 19/08/2012

Chapter was closed on October 2, 2009, after Croatian introduction of the transport network TEN-T and several projects agreed with the European Commission.

Chapter 22: Regional Policy and Coordination of Structural Instruments

European Union devotes a large part of its budget to support the development of the member-states and their regions and to encourage competitiveness among regions by diminishing of the differences between them.⁷² First projects launched on Croatian territory were those in the water supply industry, waste management or in, for instance, railway construction and the internal sailing. The advancement was approved, and the chapter was closed on April 19, 2011.

Chapter 23: Judiciary and Fundamental Rights

This chapter is related to many various issues, such as anti-corruption or human rights on both domestic and Union's territories, which are subjects to a comprehensive set of regulations, which, to be implemented correctly, require strong organization of the legal system. Such organization must encompass:

- “Judiciary
- fight against corruption and organized crime,
- fundamental rights,
- cooperation with the International Criminal Tribunal for the Former Yugoslavia (ICTY).”⁷³

For Croatia, this was one of the most challenging negotiations' chapters to be fulfilled. The country was supposed to take a broad range of reforms to harmonize its system correspondingly to the EU requirements. After a broad Judicial Reform Strategy and huge Action Plan, where all the institutions were vulnerable, Croatian judiciary became more independent, accountable, impartial, professional and more efficient.⁷⁴ Here, the extensive anticorruption campaign has been implemented and many other issues like raising the protection of minorities, better

⁷² Regional Policy and Coordination of Structural Instruments-Chapter 22, http://www.eu-referendum.hr/eu_i_mi/clanstvo22.html, accessed on 20/06/2012

⁷³ Judiciary and Fundamental Rights-Chapter 23, <http://www.delhrv.ec.europa.eu/?lang=hr&content=3156>, accessed on 10/08/2012

⁷⁴ Interim Report on Chapter 23, European Commission, 2011, http://www.delhrv.ec.europa.eu/files/file/articles-interim_report_hr_ch23_en-1299227340.pdf, accessed on 19/06/2012

protection, or tracking and better handling the domestic war crimes' issues. The chapter was closed on June 30, 2011.

Chapter 24: Justice, Freedom and Security

Due to the fact that European Union is a huge territory without internal borders, it has to dedicate extensive attention to tighten its external borders as well as to prepare future member-states to take part in such union. Future member-states, on the other hand, have to dedicate their efforts and ensure the Union that they are secure enough to take this role. This chapter is therefore in tight connection with migration, asylum, visa policy, external borders and Schengen, police cooperation, judicial cooperation in civil and criminal matters or fight against organized crime and other protection' measures. Croatia has made significant advancement in these matters and the chapter was closed on February 22, 2010.

Chapter 25: Science and Research

Providing better environment for ambitious people who largely contribute to the social and economic development is extremely important issue in the European Union. European Institute of Innovation and Technology operates as a connection of the private, research community and universities. For many ambitious Croatian people who want to share their unique knowledge, it is motivating to hear that Croatia has fulfilled the requirements and the chapter was closed already on June 12, 2006.

Chapter 26: Education and Culture

Life-long Learning Programme is the biggest project made of educational and training initiatives provided by the European Union all over Europe, where students on all levels have great opportunities for future carriers. Educational qualifications are given within the national frameworks which are interconnected with the European framework.⁷⁵ However, member-states maintain their own educational policy, supported by EU to stay favourable and competitive. As regards the culture, European initiatives are supporting continual exchange of cultural events and its development throughout Europe. Croatia has reached high level of the system' harmonization and the chapter was closed on December 11, 2006.

⁷⁵ The Lifelong Learning Programme, <http://www.lifelonglearningprogramme.org.uk/>, accessed on 28/08/2012

Chapter 27: Environment

Member-states of the European Union commonly participate in the environment protection through common policy. Issues on agenda are various, such as air quality, natural biotopes with various species, pollution etc. Croatian system of the environment protection and its high level of ecologic standards were approved by Commission and the chapter was closed on November 27, 2009.

Chapter 28: Consumer and Health Protection

Consumers throughout European Union enjoy status of very important actors on the market. They are regulators of the economic development who play an important role of the market decision-makers. They are regulators of economic development, influencing the business policies, hereby fostering the fair competition and stimulating the desirable functioning of the market.⁷⁶ Croatian level of alignment with the *acquis* of the European Union is very high. The chapter was closed on October 2, 2009.

Chapter 29: Customs Union

Regulations on Customs Union are set in the way that they are applicable in all the member-states. Their national authorities are therefore responsible to implement these regulations in real life, and provide security through fighting various kinds of threats which could harm much larger territory than the one of a single nation. Customs union is a key component providing good functioning of the European common market where high level of protection is required.⁷⁷ After Croatian entry to the European Union, borders and its customs services with Slovenia and Hungary will disappear and the ones with Bosnia and Herzegovina, Montenegro and Serbia will remain. Here, the external border of the EU will be extended. The chapter was closed on October 30, 2008.

Chapter 30: External Relations

Common trade policy of the European Union is one of the most important policies of the integration. It is consisted of set of regulations for protection of the domestic production,

⁷⁶ Consumer and Health Protection, Croatian Ministry of Economy,
<http://potrosac.mingorp.hr/hr/potrosac/clanak.php?id=12466>, accessed on 20/08/2012

⁷⁷ Customs Union-Chapter 29, http://www.eu-referendum.hr/eu_i_mi/clanstvo29.html, accessed on 20/06/2012

obligations from WTO, bilateral agreements with non-member states, whereas the tariffs are common for all the member-states. Croatia is obliged to promote and strengthen its regional cooperation as well as strengthen the political framework on bilateral level with the SEE countries, then with those outside the EU and to strengthen the public diplomacy and launch the cultural promotion' programs.⁷⁸ The chapter on Croatian external relations was closed on December 22, 2010.

Chapter 31: Foreign, Security and Defence Policy

Policies implemented in EU related to defence is one of the one of the most powerful tool for coordination of the integration among the other nations throughout the world. Within its activities, European Union constantly keeps the high level of connection with the official of the third countries, alliances and international organizations on the global and regional level and contributes to the world peace and security.⁷⁹ As their member, Republic of Croatia continuously communicates and cooperates with the United Nations, Organization for Security and Co-operation in Europe (OSCE), the council of Europe and NATO and supports the EU civilian missions and is also engaged in those in NATO missions (Afghanistan and Kosovo).⁸⁰ The chapter was successfully fulfilled and was closed on February 22, 2010.

Chapter 32: Financial Control

As one of the most powerful economies in the world, European Union must be ensured that the applicant country has taken all the necessary measures and has established well functioning supervision of the public funds or, for example, the structure for effective fight against counterfeiting of euro before it becomes the acceding country.⁸¹ Negotiations on the chapter between Croatia and European Union started on Intergovernmental Conference in June, 2007. Republic of Croatia was supposed to reach the following objectives to fulfill the commitments:

⁷⁸ Strategic Plan, Croatian Ministry of Foreign and European Affairs, http://www.mvep.hr/custompages/static/hrv/files/Strateski_plan_MVEP-a_2013-2015.pdf, accessed on 31/05/2012

⁷⁹ "Foreign, Security and Defence Policy", 2011, <http://www.vecernji.hr/vijesti/31-vanjska-sigurnosna-obrambena-politika-clanak-301227>, accessed on 05/08/2012

⁸⁰ Progress Report, European Commission, 2010, http://www.eu-pregovori.hr/files/izvijesce/Croatia_2010_Progress_Report.pdf, accessed on 16/08/2012

⁸¹ "Negotiations CRO-EU, Chapter 32, <http://www.monitor.hr/clanci/pregovori-rh-eu-poglavlje-32/152105/>, on 20/08/2012

- “Adoption and implementation of act on the system of internal financial controls in public sector (PIFC) and related policies that are supported by an adequate implementing policy;
- Maintenance of the functional and financial independence of the State Auditing Office through the alterations and supplements of the constitutional regulations or of the national legislation that is equally effective, and the adoption and implementation of the of the necessary accompanying acts;
- Alignment of Croatian Criminal Law with the Convention on the Protection of the European Communities’ Financial Interests (PIF) and its protocols;
- Establishment of the efficient and effective coordination service that guarantees fulfillment of the commitments arising from the article 280.-paragraph 3. of the Maastricht Treaty⁸² and the Council regulation No. 2185/96 on direct control and supervision of the Commission, especially in terms of Commission inspectors’ assistance, at latest from the day of accession to EU;
- Legislative and administrative harmonization with the Council regulation No. 1338/2001 regarding the measures which are necessary to protect euro from counterfeiting, and which is applicable at latest from the day of accession to EU.”⁸³

Regarding the public internal financial control (PIFC), Ministry of Finance established the Central Harmonization Unit which was responsible for implementation of PIFC, and has adopted variety of alterations in Croatian law. In terms of control of acquired education and providing of further education, in 2007 new programme was brought, on professional training for certified internal audit and the tooltip for knowledge and capabilities’ checkout, along with test provision for the certified internal audit in public sector. Furthermore, another innovation was trainings for finance management and controls’ developers for the positions on the state level. New internal auditing units were established across the country.

⁸² “Without prejudice to other provisions of this Treaty, the Member States shall coordinate their action aimed at protecting the financial interests of the Community against fraud. To this end they shall organise, together with the Commission, close and regular cooperation between the competent authorities.”, Article 280.-paragraph 3. of the Maastricht Treaty, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:12002E280:EN:HTML>, accessed on 19/06/2012

⁸³ Translated from the Report on Commitments’ Fulfillment (Chapter 32), Croatian Government, [http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/32_financijski_nadzor/poglavlje_32_izvjesce_o_ispunjenju_obveza/\(view_online\)/1](http://www.vlada.hr/hr/preuzimanja/stajalista_pregovarackog_procesa/32_financijski_nadzor/poglavlje_32_izvjesce_o_ispunjenju_obveza/(view_online)/1), accessed on 13/08/2012

Regarding the external audit, the autonomy of the State Auditing Office was increased as well as its activities; thereafter the Office implemented the revision over political parties and non-attached parliament' members and revision of the functioning of the internal financial controls' system. Judicial Academy prepared further educational programs and workshops for lawyers, such as workshops on issues related to money laundering or economic crimes.

Within the framework of anti-fraud protection of the EU's financial interests, AFCOS⁸⁴ network was established for suppression, reporting and handling frauds and doubtful activities. As for the protection of euro counterfeiting, many national centers, aimed to reveal and analyze banknotes and coins, were opened in the Croatian National Bank. All the activities resulted with European Commissions' approval and the chapter was closed on July 27, 2007.

Chapter 33: Financial and Budgetary Provisions

In European Union, the budget for 2011, counted almost EUR142 billion, of which 1% is derived from its member-states.⁸⁵ EU collects money for the member-states on the basis of their gross national incomes; therefore, the applicant country must harmonized system to implement their payments. During the accession negotiations, evaluation of the system was made by observing traditional own resources, VAT resource, GNI resource, administrative infrastructure of EU's own resources system. The chapter was closed on June 30, 2011.

Chapter 34: Institutions

This chapter was not negotiated on the regular basis. These negotiations brought decisions on Croatian position after the entry to the European Union. After the entry, Croatian language will be adopted as one of official languages of European Union. Croatia will have one seat in the European Commission, one in the Court of Justice, a seat in the General Court as well as one seat in European Court of Auditors. Furthermore, Croatia will, such as Ireland and Lithuania, occupy 12 seats in the European Parliament. Just as Denmark, Ireland, Slovakia and Finland, Croatia will have seven votes in decision-making processes and in adoption of the acts by European Council and Council of the European Union that require qualified majority. In addition, governor of the Croatian National Bank will have a seat in the Governing Council of

⁸⁴ AFCOS- Anti-fraud Coordination Structure.

⁸⁵ EU Budget, http://europa.eu/pol/financ/index_en.htm, accessed on 19/06/2012

the European Central bank. Croatia will also have nine representatives in each European Economic and Social Committee and in Committee of the Regions.⁸⁶ On November 5, 2010, EU settled all the necessary details with Croatia and the chapter was closed.

Chapter 35: Other Issues

This chapter is opened at the end of the negotiations' process as it requires discussion on the issues that may appear beside the previous chapters' issues but are not related to them and do not require any concrete reforms to be fulfilled. Croatian participation in the funds of EU or in the European Investment Bank, special regime of the customs control of Neum corridor⁸⁷ and some other related issues were negotiated. On June 30, 2011, all the relevant topics were discussed and the accession negotiations with Croatia were hereunder closed. On November 9, 2011, the Accession Treaty for the 28th EU member state was signed.

5. Croatian Pre-Accession Strategy

The negotiations' process between Croatian and the EU was not the last stop on the Croatian way to the European Union. Each of the chapters fulfilled must be the basis for the further advancement of Croatia to persist in much bigger and much more challenging environment. Even though Croatia is the first of six EU candidates that has achieved the objective, all the countries have adopted the economic programmes approved by European Commission as guidelines towards the capable EU partners. We will now see Croatian economic challenges from 2012 to 2014 in comparison with the EU candidates (Iceland, Former Yugoslav Republic of Macedonia, Montenegro, Serbia and Turkey).

The following graph demonstrates the expected budgetary statuses of Croatia and the EU candidate countries by 2014, after the extensive fiscal consolidation of each (in percent of GDP):

⁸⁶ CRO-EU Negotiations, Chapter 34, http://www.dnevno.hr/vijesti/svijet/eu/pregovori_rheu_poglavlje_34_institucije/324657.html, accessed on 19/08/2012

⁸⁷ Neum- the only coastal part of neighboring Bosnia and Herzegovina separated from Croatia with borders.

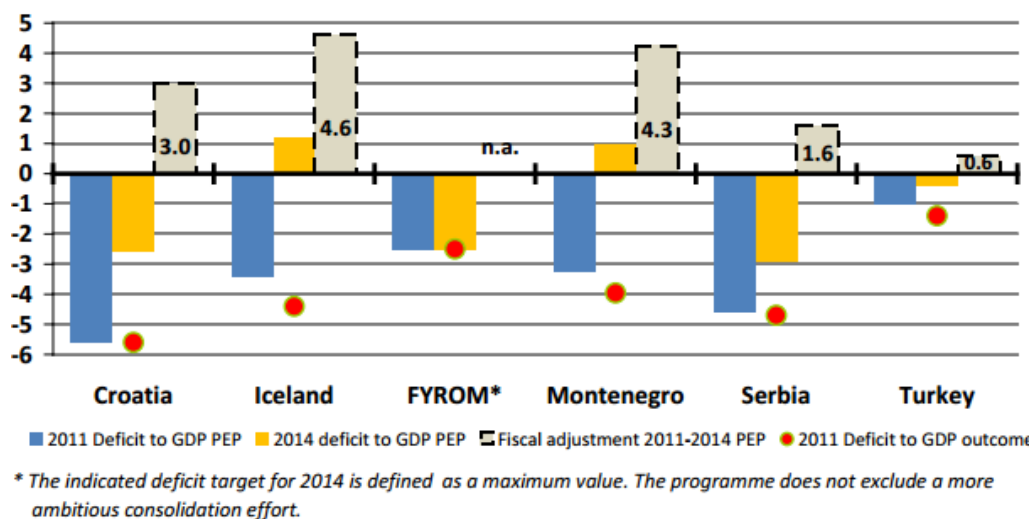


Figure 9: Budgetary Developments under PEP 2012-2014

Source: European Commission, 2012.

For Croatia, this is the country's eighth Pre-Accession Economic Programme and the first PEP for Croatia as an EU acceding country. It is crucial for the country to reach the highest competitive level possible to persist in competitive environment, meaning that it is inevitable to boost the domestic demand. Projections for 2012-2014 are tailored to meet the 0,8% growth of the real GDP in 2012, 1,5% growth in 2013 to 2,5% growth in 2014. The main drivers for GDP growth are expected to be investments from the public enterprises, whereas the private sector and government itself are not expected to make significant changes.⁸⁸ Although export markets are in the slight recession, in the beginning of 2012, Croatia registered positive movements in exports with expansion of +2,2 %, whereas imports made just +1,1%. Here, the proportion of net exports in GDP records 0,4%. For the following years it is therefore expected that the net exports will increase to 0,7% of GDP and the imports to decrease. However, there are not very positive projections for the private consumption. As the economic indicators for the beginning of 2012 were showing high, 21% unemployment rate, it is a forerunner of the low real disposable income that, on the other hand, means the decrease in the private consumption. However, the unemployment rate is expected to decrease in the following two years, meaning that there are also good projections for the real disposable income as well as the private

⁸⁸ Occasional Papers 98, European Commission, 2012, http://ec.europa.eu/economy_finance/publications/occasional_paper/2012/pdf/ocp98_en.pdf, accessed on 19/06/2012

consumption. As regards the exchange rate stability, Croatian National Bank is not changing its strategy and it keeps maintaining stable kuna against euro as it can bring the prices to the sustainable level. Therefore, kuna against euro is expected to stay around 7,47 in 2012 and 7,48 HRK/EUR is projected for the next two years. In order to successfully reach these projections, Croatia must respect the following PEP suggestions:

- “An imminent stabilisation of international macroeconomic conditions;
- quick implementation and effects of planned structural reforms;
- and improving economic sentiments.”

These suggestions can be taken as a serious motivator in the further Croatian performance, as from July 1, 2013, all the reforms will have to speed up to catch the pace of the other competitive markets. In addition, there is a mitigating circumstance in terms of reforms’ financing in the following years. Croatia will have access to the European Union’s Structural Funds and all that Croatia needs, besides the healthy and capable people, is having well structured priorities for the incoming opportunities. More than EUR1,5 billion annually will Croatia obtain from the EU Structural Funds, whereas Croatia will contribute with the amount of app. EUR680 million to the European Union. Good strategy can make Croatia not only a desirable holidays’ destination but also an attractive environment for making business and creating a competitive environment where even the most positive projections from the PEP will be easier to reach.

6. Outcomes, Analyses and Suggestions

In this paper we were mainly focused on the analysis of the economic Copenhagen criteria. However, judiciary and rule of law, which take part in the political Copenhagen criteria, are the issues closely connected to the other sectors in the economy. Even though Croatia has made a good progress in the harmonization process and attempts to provide a stable judicial system and healthy legislative environment, judiciary was the one of the most requiring chapters to be fulfilled. The message from the European Commission was that Croatia has to keep modernizing

the public services, and to make them free of the corruptive activities.⁸⁹ Deep structural reforms in every segment are the crucial point that can be derived from the Commission's notes.

Only well functioning rule of law can protect the economy from various corruptive activities. However, it is worth to take into account that the implementation of broad range of reforms can lead to the "overregulated" system, meaning that within adoption of the new acts it is necessary for the country to remove some directives which will not be relevant after introducing the new ones.

What happens in Croatia is, in my opinion, exactly the overregulated fiscal policy arising from adding new acts without cancellation of the old ones. This can lead to the situation in which enterprises are tied up with huge set of directives; therefore they cannot operate freely enough to encourage fast and efficient development. In Croatia we can find some additional payments in the form of the parafiscal taxes. These taxes, beside the regular taxes to be paid, can be very aggravating for businesses. The parafiscal taxes are related especially to the buildings construction' sector and they include:

- "one-off stamp duties (in order to issue location, construction and usage permits);
- one-off communal contribution fees; and
- one-off water contribution fees and once built, ongoing other water fees.

Or other types of the parafiscal taxes which are:

- quarterly forest contribution fees;
- monthly tourist contribution fees;
- monthly monument contribution fees; and
- monthly fees and contributions to the Croatian Chamber of Commerce.⁹⁰

As mentioned, Croatia is not the one of those economies with strong exports of goods and services which would make the country resistant to smaller deficits within the sectors. This is why Croatia would have to be careful in usage of the Union's Structural Funds. If we want to

⁸⁹ "Croatia 2011 Progress Report", European Commission, October 2011, http://ec.europa.eu/enlargement/pdf/key_documents/2011/package/hr_rapport_2011_en.pdf, pages 6 and 7, accessed on 19/06.2012

⁹⁰ Quotation from "Tax Card 2012", KPMG Croatia d.o.o., 2012, <http://www.kpmg.com/HR/en/Documents/HR%20Tax%20Card%20Eng%20WEB.pdf>, accessed on 29/08/2012

provide a useful suggestion for Croatia to make a good strategy for raising the level of production hereby stimulating the exports and competitiveness, we have to compare more than several other economies and the structures of their GDP's. For instance, in Greece, which is the most affected EU country by the global economic crisis, we can notice significant difference in the share of services in GDP (78,9% of GDP estimated in 2011) on the one hand, and shares of agriculture and industry (3,3% and 17,9% in the same year) on the other. In Spain, the services' sector contributes to the GDP with 71%, whereas the agricultural and industrial sectors contribute with 3,2% and 25,8%, according to the CIA's 2011 estimation. On the other side we have Czech Republic and Hungary; the two countries displaying more resistance in crisis. In Czech Republic the industrial sector occupies even 38,1%, agricultural 1,6%, whereas services' sector has 60,3% of share in the country's GDP according to the same data. In Hungary we can see that agriculture and industry occupy 3,7% and 31,3% of its GDP, whereas 65% of GDP is composed of services.⁹¹ From these data we can conclude that those countries which are not the world's strongest economies but have been less affected by the crisis, have invested more in the agricultural and industrial sector, hereby balancing the structure of GDP. Exactly this point can be used as a strategy proposal for Croatia, where the GDP is reflecting that 5,4% of the GDP goes to the agriculture, 25,5% of GDP is occupied by industrial sector and 69,1% of GDP is composed of the services' sector.⁹² This analysis shows that in order to increase productivity of the material goods, Croatia would have to use European Structural Funds with tendency to reach 35%, if not 40% of GDP composed of both agricultural and industrial sectors.

As regards the candidate countries for the European Union, the suggestion would be to stay patient in the attempts to harmonize their systems. From the previous chapters we could understand how long and uncertain this process can be but, still, persistence can overbear the existing obstacles. Warnings and suggestions for Croatian strategy, as explained in this chapter, can be applied not just in the candidate countries, but also in all the other countries that need to make some changes in their economies.

⁹¹ The World Factbook, "GDP-Composition by Sector", Central Intelligence Agency, <https://www.cia.gov/library/publications/the-world-factbook/fields/2012.html>, accessed on 29/08/2012

⁹² The World Factbook, "GDP-Composition by Sector", Central Intelligence Agency, <https://www.cia.gov/library/publications/the-world-factbook/fields/2012.html>, accessed on 29/08/2012

Conclusion

Creating such community as European Union was greeted with a huge applause and the entity itself is enviably well organized. Its aim is to work in favor of a global prosperity by creating common market, being truly fair play oriented and, still, very competitive. With introduction of euro as a common currency, one could have expected that the market was going to be sealed and indestructible. However, although the concept is comprehensive enough to justify little obstacles in the strategies' implementations, nowadays European Union is facing much bigger problems than just everyday squabbling over the ordinary topics. Euro is in the middle of the financial turmoil where the exit seems to be out of anyone's reach. Anyway, although EU politicians had quite hard decisions to make and large amounts of money was sacrificed for the affected countries' bailouts; they keep on being optimistic and enthusiastic in their attempts to save the eurozone. In my opinion, they act as the real leaders, persistent, willful and brave. However, it seems that the situation is too risky to stay just optimistic and willful.

As regards Croatia, the country will probably not enter the eurozone very soon after the entry to the EU, as it still has some issues to meet the necessary criteria. Furthermore, Croatia has not been in the good economic position in the recent past years. In my opinion, Croatia is, despite the fact that it is currently handling hard recession with high unemployment rate and decreased consumption, still somehow protected from the possible outcomes of euro crisis. The fact is that on July 1st, 2013, many other doors will be opened for Croatian citizens, which can open new perspectives on the future employment or educational opportunities, whereas eurozone will still be far away and the possible negative outcomes of euro would not be the primary issue for now. As long as Croatia varies among the deep recession and a bit lessen recession which is, of course, largely enhanced by external trends, it should first work on the overall consolidation.

Croatia should not, in my opinion, be too fascinated by the fact that in the near future it will be able to take part in the European Funds' usage. It has to focus on the creation of the new values within society and start to work on diverting the spending in different areas, starting

with encouraging production sector if it wants to reach further advancement. As mentioned, the country had to deal with a plenty of issues given by European Union and it succeeded. Therefore, it should take the recent future as a motivating factor to work more.

In my opinion, Croatians can largely thank its central bank for intervening in crucial moments by continuous efforts to keep the exchange rate stable. Moreover, the Bank had launched many initiatives to encourage Croatian citizens to persist in the crisis. This is why I think, that the Croatian managed exchange rate regime along with the alienation of the governmental influence on the Bank, is a good system for now. However, the stabilization of the system as a whole needs to be generated by sharp increase in production, as this is not a right time to wait for the miracles to happen. According to my opinion, one of the biggest worship of the European Union was encouraging Croatia to zoom out the influence of the government on the public sector where the private sphere became more distant. This is the only way for the enterprises to feel worried about their future and a powerful motivator in their future moves. Only this can generate creation of the healthy and competitive environment and make Croatia exhibit its power not only in the country but also abroad. This is also a great sign for the neighboring countries as it can increase the overall regional cooperation and boost the regional prosperity. I still think that Croatia has much to offer and contribute to the European Union. Still, only time can reveal where the real countries' priorities will be directed.

The objective of this paper was to make a comprehensive elaboration of the Croatian attempts to meet the requirements of the European Union in order to come with some useful solutions not only for Croatia but also for the other countries, to become the Union's reliable partners in the future matters. The paper provides an examination of a wide range of Croatian strengths and weaknesses in the period of the accession process to the European Union which has brought us to the point from which we have been ready to give the suitable solutions and suggestions.

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ANNEX

Public Dept						
At the End of	2005	2006	2007	2008	2009	2010
the Period (In HRK Millions)						
1 . I n t e r n a l P u b l i c D e b t	56.120,2	60.851,5	64.811,6	69.857,1	80.331,9	91.455,6
1.1. Internal Croatian	50.839,3	50.839,3	56.882,0	64.959,6	74.470,9	85.123,2
Debt						
Treasury Bills	12.278,0	12.412,9	11.740,6	14.440,7	18.802,5	20.225,9
Instruments of Money						
Market	0,9			10,7	19,3	20,5
Bonds	31.151,8	35.249,6	39.273,5	39.306,7	39.369,3	48.190,4
Bank Loans	7.408,6	6.827,0	5.867,9	11.201,5	16.279,8	16.686,4
1.2. Internal Debt of						
Republic's Funds	3.953,5	5.198,0	6.357,8	3.035,0	3.794,4	4.385,8
Instruments of Money						
Market	-	-	-	-	-	-
Bonds	-	-	-	-	-	-
Bank Loans	3.953,5	5.198,0	6.357,8	3.035,0	3.794,4	4.385,8
1.3.Internal Debt-Local						
State Level	1.327,4	1.164,0	1.571,8	1.862,5	2.066,6	1.946,5
Instruments of Money						
Market	40,7	29,3	36,8	12,0	6,8	1,6
Bonds	185,1	294,2	472,3	582,7	574,6	550,1
Bank Loans	1.101,6	840,5	1.062,7	1.267,8	1.485,2	1.394,8
2. External Public Debt	45.363,6	41.660,5	39.658,2	30.286,8	37.510,1	42.482,2
2.1.External Croatian	36.414,5	32.556,6	29.424,0	28.459,4	35.785,8	40.761,5
Debt						
Instruments of Money	-	-	-	-	-	-
Market						
Bonds	27.020,1	22.836,9	20.397,3	18.768,2	26.101,8	29.468,0
Loans	9.394,5	9.719,7	9.026,7	9.691,2	9.684,0	11.293,5
2.2.External Debt of	8.749,8	8.938,2	10.186,7	1.800,3	1.715,3	1.715,3
Republic's Funds						
Instruments of Money	-	-	-	-	-	-
Market						
Bonds	-	-	-	-	-	-
Loans	8.749,8	8.938,2	10.186,7	1.800,3	1.715,1	1.683,3
2.3.External Debt-Local	199,3	165,7	47,5	27,1	9,0	5,4
State Level						

Instruments of Money	-	-	-	-	-	-
Market						
Bonds	-	-	-	-	-	-
Loans	199,3	165,7	47,5	27,1	9,0	5,4
T o t a l P u b l i c D e b t (1 + 2)	101.483,7	102.512,0	104.469,8	100.143,9	117.842,0	133.937,7
GDP	264.367,0	286.341,0	314.223,0	342.159,0	333.063,0	331.498,0
P u b l i c D e b t (% G D P)	38,4%	35,8%	33,2%	29,3%	35,4%	40,4%

- **Table 1: Structure of Public Debt 2005-2010**

Source: Croatian Ministry of Finance, 2010

