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NOTE

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

Delegations will find attached the above-mentioned draft Council Recommendation, as revised and agreed by various Council committees and finalised by the Economic and Financial Committee, based on the Commission Proposal COM(2026) 211 final.

COUNCIL RECOMMENDATION

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

THE COUNCIL OF THE EUROPEAN UNION,

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

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

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

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

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

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1 Regulation (EU) 2024/1263 of the European Parliament and of the Council of 29 April 2024 on the effective coordination of economic policies and on multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97 (OJ L, 2024/1263, 30.4.2024, ELI: http://data.europa.eu/eli/reg/2024/1263/oj).

Whereas:

(1) Regulation (EU) 2024/1263 specifies the objectives of the economic governance framework, which aims at promoting sound and sustainable public finances, sustainable and inclusive growth and resilience through reforms and investments, as well as preventing excessive government deficits. The Regulation stipulates that the Council and the Commission conduct multilateral surveillance in the context of the European Semester in accordance with the objectives and requirements set out in the Treaty on the Functioning of the European Union (TFEU). The European Semester includes, in particular, the formulation and the surveillance of the implementation of country-specific recommendations.

(2) On 25 November 2025, the Commission adopted an opinion on the 2026 draft budgetary plan of Croatia. On the same date, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the 2026 Alert Mechanism Report, in which it did not identify Croatia as one of the Member States for which an in-depth review would be needed. The Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area, a recommendation for a Council recommendation on human capital in the European Union, and a proposal for the 2026 Joint Employment Report, which analyses the implementation of the Employment Guidelines and the principles of the European Pillar of Social Rights. The Council adopted the Recommendation on the economic policy of the euro area[2] on 21 April 2026 and the Joint Employment Report, as well as the recommendation on human capital on 9 March 2026.

(3) On 29 January 2025, the Commission published the Competitiveness Compass, a strategic framework that aims to boost the Union's global competitiveness over the next five years. Since its publication, the Competitiveness Compass has informed the work of the European Semester, ensuring that Member States' economic policies are consistent with the EU's strategic objectives, creating a unified approach to economic governance that fosters sustainable growth, innovation and resilience across the Union.

[2] OJ C, C/2026/2434, 28.4.2026, ELI: http://data.europa.eu/eli/C/2026/2434/oj.

(4) In 2026, the European Semester for economic policy coordination continues to develop alongside the final stage of Recovery and Resilience Facility (RRF) implementation[3]. Recovery and resilience plans (RRPs), along with cohesion policy funding, have been essential for delivering on the policy priorities under the European Semester, as the plans were required to effectively address all or a significant subset of challenges identified in the relevant country-specific recommendations issued in recent cycles, and programmes funded by the European cohesion policy were required to take country-specific recommendations into account. As the RRF approaches the end of its lifetime, it remains essential to sustain and build on the reforms and investments supported and implemented under the RRF, in particular those that contribute to addressing challenges identified in the country-specific recommendations.

(5) On 3 June 2026, the Commission published the 2026 country report for Croatia. It assessed Croatia's progress in addressing the 2025 country-specific recommendations and took stock of Croatia 's implementation of the RRP. On the basis of that analysis, the country report identified the most pressing challenges Croatia is facing. It also assessed Croatia's progress in implementing the European Pillar of Social Rights and in achieving the Union headline targets on employment, skills and poverty and social exclusion reduction, as well as progress in achieving the United Nations Sustainable Development Goals.

[3] Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility (OJ L 57, 18.2.2021, p. 17, ELI: http://data.europa.eu/eli/reg/2021/241/oj).

(6) On 21 January 2025, the Council, upon the assessment and recommendation of the Commission, adopted a Recommendation endorsing the national medium-term fiscal-structural plan of Croatia[4]. The plan covers the period from 2025 until 2028 and presents a fiscal adjustment spread over four years. The Council recommended the following maximum growth rates of net expenditure: 6.4% in 2025, 4.9% in 2026, 4.1% in 2027 and 3.7% in 2028, which correspond to the maximum cumulative growth rates calculated by reference to the base year of 2023 of 26.2% in 2025, 32.3% in 2026, 37.8% in 2027 and 42.9% in 2028.

(7) Russia's war of aggression against Ukraine and its repercussions constitute an existential challenge for the European Union. The Commission has invited Member States to request the activation of the national escape clause of the Stability and Growth Pact in a coordinated manner to support the EU efforts to achieve a rapid and significant increase in defence spending[5] and this proposal was welcomed by the European Council of 6 March 2025. Following the request of Croatia, on 8 July 2025 the Council, upon a recommendation from the Commission, adopted a Recommendation allowing Croatia to deviate from the recommended maximum growth rates of net expenditure[6]. The period when the national escape clause is activated (2025-2028) allows Croatia to reprioritise government expenditure or increase government revenue so that lastingly higher defence expenditure would not endanger fiscal sustainability in the medium term.

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[4] Council Recommendation of 21 January 2025 endorsing the national medium-term fiscal-structural plan of Croatia (OJ C, C/2025/638, 10 February 2025, ELI: https://eur-lex.europa.eu/eli/C/2025/638/oj).

[5] Communication from the Commission, 'Accommodating increased defence expenditure within the Stability and Growth Pact', Brussels, 19 March 2025, C(2025) 2000 final.

[6] Council Recommendation of 8 July 2025 allowing Croatia to deviate from the maximum growth rates of net expenditure as set by the Council under Regulation (EU) 2024/1263 (Activation of the national escape clause), (OJ C, C/2025/3967, 20 August 2025, ELI: http://data.europa.eu/eli/C/2025/3967/oj).

(8) On 7 May 2026, Croatia submitted its 2026 Annual Progress Report[7] on adherence to the recommended maximum growth rates of net expenditure and the implementation of reforms and investments responding to the main challenges identified in the European Semester country-specific recommendations. The Annual Progress Report also reflects Croatia's biannual reporting on the progress made in implementing its recovery and resilience plan in accordance with Article 27 of Regulation (EU) 2021/241.

(9) Real GDP growth in 2025 was 3.4% and HICP inflation stood at 4.4%. The Commission Spring 2026 Forecast projects real GDP to grow by 2.7% in 2026 and 2.5% in 2027, and HICP inflation to stand at 4.6% in 2026 and 2.7% in 2027.

(10) Based on data provided by Eurostat[8], Croatia's general government deficit increased from 2.3% of GDP in 2024 to 3.0% in 2025. The increase in the deficit in 2025 mainly reflects an increase in nationally financed investments, public wages and social assistance expenditure. Based on policy measures known by the cut-off date of the forecast, the Commission Spring 2026 Forecast projects a deficit of 2.9% of GDP in 2026 and 2.7% of GDP in 2027.

(11) Based on the Commission's estimates, the fiscal stance[9], which includes both nationally and EU financed expenditure, was expansionary, by 1.6% of GDP, in 2025. It is projected to be contractionary in both 2026 and 2027, by 0.3% and 0.9% of GDP, respectively.

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7 The 2026 Annual Progress Reports are available on: https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/stability-and-growth-pact/preventive-arm/annual-progress-reports_en.

8 Eurostat-Euro Indicators, 22 April 2026.

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

(12) Based on data provided by Eurostat[10], Croatia's general government debt decreased from 57.4% of GDP at the end of 2024 to 56.3% of GDP at the end of 2025. Based on policy measures known at the cut-off date of the forecast, the Commission Spring 2026 Forecast projects the debt-to-GDP ratio to decrease to 55.9% by the end of 2026 and to further decrease to 55.6% by the end of 2027.

(13) Based on Eurostat data[11], total general government defence expenditure in Croatia amounted to 1.5% of GDP in 2025, corresponding to an increase of 0.5 percentage points of GDP compared to the reference year 2021. According to the Commission Spring 2026 Forecast, it is projected at 1.6% of GDP in 2026, corresponding to an increase of 0.6 percentage points of GDP compared to 2021[12].

(14) The Union continues to face risks of energy supply disruptions and elevated price volatility, exacerbated by geopolitical tensions which affect global oil and gas markets. Experience from the 2022–2023 energy crisis has shown that broad and untargeted measures entail large fiscal costs and are socially and economically inefficient. Since the outbreak of the war in the Middle East in February 2026, Croatia adopted fiscal policy measures to mitigate the impact of high energy prices on households and firms[13]. These include an untargeted reduction in excise duty on diesel due to expire on 18 May 2026, as well as targeted support for public passenger transport, agriculture, fisheries, aquaculture and for energy-intensive industry expiring on 30 September 2026. According to the Commission Spring 2026 Forecast, the fiscal cost of these measures is projected to amount to 0.1% of GDP in 2026. According to Commission estimates, if these measures were to remain in force until end-2026, their fiscal cost would amount to 0.2% of GDP in 2026.

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10 Eurostat-Euro Indicators, 22 April 2026.

11 Eurostat, government expenditure by classification of functions of government (COFOG).

12 The NATO defence spending definition differs from the COFOG defence definition. Furthermore, there could be differences due to the time of recording of expenditure, in particular military equipment, as the NATO reporting does not follow national accounts rules for the time of recording.

13 This reflects the situation at the cut-off date of the Commission's Spring 2026 Forecast (4 May 2026).

(15) Based on Commission calculations, net expenditure in Croatia grew by 10.9% in 2025 and 30.1% cumulatively over 2024 and 2025. The net expenditure growth in 2025 is above the recommended maximum growth rate, corresponding to a deviation of 1.8% of GDP in annual terms. When considering 2024 and 2025 together, the cumulative growth rate of net expenditure is also above the recommended maximum growth rate, corresponding to a deviation of 1.4% of GDP in cumulative terms. Taking into account the flexibility for higher defence spending provided for by the national escape clause, the cumulative deviation of net expenditure amounts to 0.9% of GDP.

(16) Based on Commission calculations, net expenditure in Croatia is projected to grow by 5.7% in 2026, and 37.5% cumulatively over 2024, 2025 and 2026. The projected net expenditure growth in 2026 is above the recommended maximum growth rate, corresponding to a deviation of marginally above 0.3% of GDP in annual terms. When considering 2024, 2025 and 2026 together, the projected cumulative growth rate of net expenditure is also above the recommended maximum growth rate, corresponding to a deviation of 1.6% of GDP in cumulative terms. Taking into account the flexibility for higher defence spending provided for by the national escape clause, considering 2024, 2025 and 2026 together, the projected cumulative deviation of net expenditure amounts to 1.0% of GDP.

(17) In the coming years public finances will come under increasing pressure from rising spending needs for productive investments, population ageing, climate adaptation, defence, the twin transition, and other competing priorities. For this reason, it is warranted for Croatia to improve the quality and efficiency of public spending and the prioritisation of growth-enhancing investments, including at local level. While Croatia has made progress in strengthening its fiscal framework, including through the establishment of a spending review unit within the Ministry of Finance in 2022, the scope and transparency of spending reviews remain limited. Spending reviews are recognised as a useful tool for identifying efficiency gains and programme overlaps and the savings made as a result could be reallocated to address new emerging fiscal challenges, as the ones highlighted above. Health and education are sectors where Croatia could expand the use of spending reviews, as expenditures are relatively high, but outcomes comparatively lower than peer member states.
A comprehensive review of public administration workforce management is also warranted, given rising public employment alongside persistent understaffing in critical central government functions. This suggests ineffective resource allocation that could be addressed through targeted workforce optimisation and strategic redeployment. Croatia also has overall low insurance coverage to climate risks. Due to this, compensation is granted on an ad hoc basis. To further ensure adequate funding, Croatia could further integrate climate related fiscal risks in the budgetary planning.

(18) The introduction of mandatory e-invoicing in January 2026 under the Fiscalisation 2.0 reform and the ongoing digital transformation of the tax administration will contribute to improving tax compliance and reducing the shadow economy, with positive trends already visible in the Q1 2026 data. At the same time, Croatia foregoes a significant amount of revenues due to tax expenditures, which amounted to over 4% of GDP in 2023. Moreover, tax expenditures are not always effective in pursuing their intended policy objectives. For example, personal income tax expenditures, in particular the family allowance, seem to benefit more high-wage income earners. Value-added tax (VAT) expenditures can also be inefficient and poorly targeted at reducing inequality, in particular the VAT reduced rate for hotels and restaurants has a regressive impact. Finally, complex conditions can undermine the effectiveness of corporate income tax expenditures, pointing to scope to simplify certain tax expenditures and their administration. Croatia would benefit from a comprehensive review of tax expenditures to identify and redesign those that do not effectively achieve their intended policy objectives, including income redistribution or environmental incentives.

(19) Croatia could more broadly enhance the effectiveness and progressivity of the tax system, including by strengthening the design of property taxation. Important steps have been taken with recent reforms of immovable property taxation. However, the current framework remains limited in scope, as it applies only to vacant and secondary properties and is predominantly based on location and size rather than market value. Introducing a market value-based component and progressively broadening the tax base to cover a wider range of properties, while duly taking into account taxpayers' ability to pay, would contribute to increasing revenues and ensuring a more equitable and efficient allocation of the tax burden. It would also strengthen incentives to bring unoccupied dwellings onto the housing market.

(20) The systematic, meaningful and timely involvement of local and regional authorities, social partners, civil society and other relevant stakeholders remains essential in order to ensure broad ownership for the successful implementation of the Union's funding instruments, as well as in the context of the European Semester.

(21) The implementation of cohesion policy programmes, which encompass support from the European Regional Development Fund (ERDF), the Just Transition Fund (JTF), the European Social Fund Plus (ESF+) and the Cohesion Fund (CF) in Croatia, is above the average pace at EU level, both in terms of project selection and payments. It is important to keep current momentum, while maximising the impact of investments on the ground. Croatia is already taking action under its cohesion policy programmes to boost competitiveness and growth. Nevertheless, some areas may require further strengthening, including those relating to social inclusion, deinstitutionalisation, decarbonisation of transport and renewable energy deployment as well as circular economy. At the same time, Croatia needs to accelerate implementation of the JTF as resources are due for disbursement by the end of 2026. It is essential to ensure that the new investments identified by Croatia in its mid-term review of the cohesion policy funds, notably those linked to the five priorities identified in the Mid-Term Review Regulation[14], are deployed rapidly and effectively.

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[14] Regulation (EU) 2025/1914 of the European Parliament and of the Council of 18 September 2025 amending Regulations (EU) 2021/1058 and (EU) 2021/1056 as regards specific measures to address strategic challenges in the context of the mid-term review.

(22) Croatia faces challenges on multiple interconnected fronts, including a fragmented public research and innovation sector, complex governance structures, and a business environment weighed down by regulatory burdens, lengthy permitting processes, and the longest business-to-business payment periods in the EU. Digital infrastructure in rural and island areas lags behind EU averages. Progress on circular economy, building renovation, and renewable energy rollout remains limited, compounded by fragmented administrative procedures. On the social side, poverty and income inequality remain high, labour and skills shortages persist across sectors, healthcare access is uneven particularly in rural areas, and housing affordability continues to be a concern, especially in major cities and coastal regions.

(23) Croatia's research and innovation (R&I) performance continues to improve, but progress is hindered by persistent structural challenges, in particular the highly fragmented public R&I sector. The large number of these entities dilutes resources and hinders collaboration, resulting in lower research outputs and reduced scope for business-academia collaboration and technology transfer. Governance of the R&I system remains complex, with policy responsibilities spread across multiple entities, creating challenges for planning and implementation. Although Croatia has been implementing reforms under the recovery and resilience plan to reduce the number of public research institutions, increasing the scope, ambition and pace of implementation of these efforts would be beneficial. Regional disparities in terms of R&I performance persist, with most R&I activities carried out in Zagreb, while dedicated support to selected regional hubs, including a strong link to the industrial transition, would help improve performance in other regions. The level of public R&D expenditure as a share of GDP remains below the EU average and has been stagnating in recent years. The share of business expenditure for R&D and the uptake of innovation schemes by businesses also remains well below the EU average, especially in some regions, contributing to suboptimal performance and low productivity in the manufacturing industry. Public support for business R&D is limited and fragmented, and technology transfer activities continue to be on the low side.

(24) Croatia's financing landscape is still predominantly supported by banks, with market-based finance, including household savings via capital markets, playing a comparatively smaller role in firms' financing due to still low levels of direct retail participation, despite some recent positive momentum including successful IPOs on the Zagreb Stock Exchange and retail investor interest in government securities. Domestic institutional investors, such as pension funds and insurers, assume a limited role in financing innovative businesses. The relatively small size and liquidity of the domestic capital markets and growing but limited venture capital and private equity funding compound the financing gap for innovative firms. Reforms under the recovery and resilience plan, including the strategic framework for capital markets development, seek to promote diversification of financing options. Further progress is needed in boosting the participation of retail investors in the capital market through enhanced financial literacy and more accessible investment products, improving the venture capital and private equity environment, including incentivising participation of institutional investors, and enhancing stock market attractiveness and the overall investment environment through better corporate governance for listed companies.

(25) As set in the Competitiveness Compass, all the EU, national, and local institutions must make a major effort to produce simpler rules and to accelerate the speed of administrative procedures. The Commission has set ambitious goals for reducing administrative burden: by at least 25% for all companies and by at least 35% for SMEs. It has also created new tools to achieve these goals, including systematic stress test of the stock of EU legislation and enhanced stakeholders' dialogue. In Croatia, the complexity of administrative procedures is reported to be a constraint by 66% of companies when doing business in Croatia. Structural challenges continue to weigh on Croatia's business environment, with labour and skills shortages, regulatory complexity, and administrative inefficiencies acting as major constraints on investment and growth. Permitting processes remain particularly burdensome with lengthy timelines for construction and environmental permits, including for plant construction and decarbonisation projects in the manufacturing industry, together with fragmented procedures across authorities and limited interoperability of digital registries. Late payments between businesses have worsened, with Croatia recording the longest average business-to-business payment period in the EU. Measures in the recovery and resilience plan to digitalise public administration, promote competition, and simplify procedures are significant steps forward. However, increasing the scope, ambition and pace of regulatory simplification and administrative modernisation would be beneficial.

(26) Further progress is also needed on the efficiency of the justice system, as proceedings in civil and commercial courts remain among the longest in the EU. During recent years, Croatia has advanced with reforms and investments, including on the digitalisation of justice, strongly supported by the recovery and resilience plan. Still, Croatia remains among the Member States with the most significant backlog and duration of civil and commercial cases. As this impacts the business environment and competitiveness, it would be beneficial if Croatia continued to improve the efficiency in resolving civil and commercial court cases, in particular by implementing additional reforms, including through possible case management reforms.

(27) Croatia's territorial fragmentation affects the efficiency of its public administration and exacerbates regional disparities. There is an imbalance between responsibilities and resources, as well as the administrative and financial capacity at local level to absorb funding and deliver quality services. This contributes to the uneven quality of public services provided and raises administrative costs as many small local governments lack adequate financial and administrative resources to provide services. Although measures under the recovery and resilience plan provided financial incentives to stimulate mergers of local government units, the uptake of these incentives remains mainly focused on mergers of functions, with limited impact on actual mergers. Increasing the scope of incentives, coupled with potential legislative steps to ensure the uptake of actual mergers, would be beneficial. Furthermore, translating to the local level the national level efforts such as introducing a transparent remuneration system as well as a competency-based recruitment and promotion could help improve the quality of public services.

(28) Broadband coverage in rural and island areas still lags behind EU averages. Although the share of Croatian firms citing digital infrastructure as an obstacle fell to 36% in 2025, very high-capacity network (VHCN) coverage (78.9%) and rural VHCN (49.1%) remain below the EU averages of 82.5% and 61.9%, respectively. A significant gap persists in rural Fiber to the Premises (FTTP), which at 44.4% remains well below the EU average of 58.8%, and in 5G mid-band coverage, which reaches only 8.5% in rural areas compared to the EU's 26.2%. Setbacks in implementing projects on broadband and backhaul infrastructure to rural and suburban settlements, coupled with a remaining funding gap and structural bottlenecks, such as complex permitting procedures, spatial planning constraints, and unresolved legacy infrastructure issues, delay the digital transition.

(29) In 2025, Croatia had the sixth highest wholesale electricity price in the EU, holding back cost competitiveness, decarbonisation and electrification. Installed solar capacity has grown strongly, yet the share of solar energy in electricity generation remains low at less than 8%. Against this background, faster roll-out of new renewable energy capacity and non-fossil flexibility solutions could help reduce high electricity wholesale prices. On 27 April 2026, the Croatian energy regulatory authority adopted updated grid connection fees, which could speed up the deployment of renewable energy. Further support for the deployment of renewable energy, including green hydrogen, could help reduce the high greenhouse gas intensity of Croatia's industry, especially if part of a coherent set of industry decarbonisation measures that includes, amongst others, also carbon capture and storage and the promotion of demand for low-carbon industrial products. Increased investment in the electricity grid beyond the investments included in the Croatian recovery and resilience plan will be crucial to promote the uptake of renewable energy in Croatia. In the short term, this will require measures to incentivise hybrid storage and renewable energy projects. By 2024, 34% of household consumers had smart meters installed, which is significantly less than the EU target of 80%. To be able to fully capitalise on the increased uptake of renewable energy, significant funding for the rollout of smart meters beyond the measures in the recovery and resilience plan, as well as dynamic contracts, will be needed to empower consumers and foster demand response. Limited steps have been taken to streamline administrative procedures for renewable energy as part of the Renewable Energy Sources Act in 2025, but permitting and grid connection procedures remain fragmented and, in some cases, unclear. Further streamlining of permitting and grid connection could also help with the rollout of photovoltaic systems on multi-apartment buildings as well as energy communities, since the uptake remains negligible and procedures cumbersome.

(30) Energy efficiency measures are necessary to maintain the positive momentum created by the EU funding framework and accelerate progress in: (i) building renovation; (ii) the supply of energy-efficient housing, in particular affordable and social housing; and (iii) the replacement of gas and oil boilers with heat pumps and other more efficient and green solutions. However, increased efforts are needed beyond EU funding to achieve the building decarbonisation targets, given the large share of the building stock that still requires renovation, especially when it comes to multi-apartment buildings. Renovation programmes are primarily delivered through grants, leaving a significant private investment gap, contributing to limited residential energy savings between 2019 and 2024. Therefore, reducing overall reliance on grants and shifting to financial instruments can maximise the impact of public funds, while grant support could be better targeted to the most vulnerable households and energy inefficient buildings.

(31) Road transport is the most used mode of transport in Croatia for both passengers and freight, and its emissions have increased by 42% since 2005, one of the biggest increases in the EU. Reforms and investments under the Croatian recovery and resilience plan and cohesion policy already contribute to modernising railway infrastructure, promoting green transport, and deploying intelligent transport systems. Nevertheless, sustained efforts remain necessary. Modernising the transport infrastructure and the railway rolling stock, increasing the use of public transport and further greening it, integrating different transport modes in urban areas, promoting active mobility, putting in place intelligent transport systems, can greatly contribute to the decarbonisation of the transport sector, reduce the reliance on fossil fuels and reduce air pollution in urban centres. Promoting the uptake of zero-emission vehicles, including through targeted taxation incentives for company cars and strengthening charging infrastructure in urban areas to make it better functioning, affordable and accessible, could help to increase the share of electric vehicles, which in 2025 remained one of the lowest in the EU. In 2024, Croatia had by far the lowest share of renewable energy in transport in the EU, following a decline in 2022 due to rules for biofuels that reduced penalties for fuel suppliers for not blending biofuels into transport fuels. This temporary reduction of penalties expired as of January 2026, which is expected to help revert the recent decline in the share of renewable energy in transport. Fossil-fuel subsidies that address neither energy poverty in a targeted way nor genuine energy security concerns, hinder electrification and are not crucial for industrial competitiveness could be considered a phase-out priority. In Croatia, fossil-fuel subsidies including the reimposed emergency price cap on petroleum products introduced in March 2026 on service stations off highways**,** as well as partial refunds of excise duties for diesel in commercial transport are economically inefficient, perpetuate reliance on fossil fuels and disincentivise electrification and the shift to zero-emission vehicles and other sustainable solutions.

(32) Considering its exposure to climate-related risks and their increasing economic impact, Croatia would also benefit from swift implementation, better coordination and systematic monitoring of climate adaptation and sustainable water management policies, across sectors and levels, based on nature-based and climate-proof investments in strategic/critical infrastructure, including in coastal and island areas. As insurance coverage against weather-related and climate-related events remains one of the lowest in the EU at around 2%, there is a need to create stronger incentives for climate risk insurance, in particular regarding floods and fires.

(33) Progress towards a circular economy remains slow, with high landfilling rates, significant differences at county level separate municipal waste collection, delays in waste management infrastructure completion, and circular material use well below the EU average. While Croatia is gradually improving its strategic and legal framework to improve waste management and the circular economy, implementation is still lagging, with a negative impact both on the environment and competitiveness. There is a need to improve the circular material use rate to reduce the impact of material use on the environment while increasing Croatia's strategic independence from imported raw materials. It would also be beneficial if Croatia invests more into repair and reuse centres and to adopt measures, incentives or tax benefits to integrate secondary raw materials into new products.

(34) In light of the crucial role of human capital in enhancing the Union's competitiveness and strategic autonomy, in 2026 the Council recommended that Member States take action to urgently address human capital-related structural challenges in the areas of skills, education and training, which hamper competitiveness. The 2026 country-specific recommendations addressed to Croatia can contribute to the implementation of the Council Recommendation on human capital in the Union.

(35) Positive trends in Croatia's labour market continue, though persistent structural and regional challenges weigh on competitiveness and growth potential. Labour and skills shortages are reported across many sectors. While the employment rate has reached a record high, closing the gap to the EU average and approaching Croatia's 2030 target, it remains particularly low for vulnerable groups such as older people, low-skilled workers, and persons with disabilities. The disability employment gap also remains one of the highest in the EU. Regional disparities in labour market participation remain substantial. Limited participation in adult learning, especially outside major urban centres, constrains labour-market-relevant skills and contributes to skills mismatches, which remain above the EU average. Croatia is implementing measures to address labour market needs, supported by the recovery and resilience plan and the European Social Fund Plus. These measures include active labour market policies, upskilling and reskilling programmes, and reforms to better integrate foreign workers into the labour market. However, these efforts should be intensified and made more effective by better targeting vulnerable groups, addressing training gaps and ensuring alignment of training to the labour market needs, incentivising adult learning participation and improving labour-market-relevant skills, including through high-quality curricula at various levels of education. Fully implementing the education system reform is essential to achieve higher participation in early childhood education and care (ECEC) and more instruction time in schools, to strengthen basic skills and provide a better basis for further education and skills acquisition. Delays in completing the necessary infrastructure prevent timely implementation of full-day teaching model which should increase instruction hours and improve basic skills, while evaluation on the progress of experimental implementation remains absent. Continued efforts are needed to increase the share of qualified teachers, in particular ECEC teachers and teachers of physics and other science, technology, engineering and mathematics (STEM) subjects, to address persistent teacher shortages that risk undermining education quality, especially in remote and rural areas.

(36) Despite progress and policy efforts, Croatia faces significant social challenges. Poverty and income inequality rates have decreased for some groups, notably children, but remain high, particularly among older people, persons with disabilities and those living in rural areas and progress towards the 2030 national poverty reduction target is slow. The impact of social transfers, excluding pensions, on poverty reduction is among the weakest in the EU, and the adequacy and coverage of minimum income schemes and unemployment benefits remain limited. Recent amendments to the pension act, including a more favourable indexation formula, the introduction of an annual pension supplement, increases in the minimum pension and benefits for longer working lives, should contribute to improving pension adequacy. Access to long-term care remains insufficient, with limited access to home-based and community-based care relative to rising demand, high out-of-pocket costs, and unmet care needs among older people that are among the highest in the EU. This places disproportionate care burdens on informal carers, especially women, reducing their labour market participation. Addressing these challenges would contribute to upward social convergence.

(37) Efforts on addressing sustainability, availability and quality of healthcare are ongoing, but remain slow to translate into improved health outcomes and could be better targeted, while prevention has received limited attention. Uneven distribution of health workers remains a major barrier to healthcare access in islands, remote and rural areas. Addressing workforce shortages requires increasing the number of healthcare workers, and improving training, recruitment and retention, with particular attention to geographical disparities.
While e-health is being strengthened, the share of population using online health services remains one of the lowest in the EU. Preventable mortality has only slightly decreased over the past decade and requires better targeted measures on key behavioural risk factors, and enhanced coordination across public administration beyond the health sector, to prevent or delay the onset of diseases.

(38) Housing affordability in Croatia remains a concern. Supply is constrained by a high share of vacant dwellings and short-term rentals, especially in the main cities and coastal areas, with price increases broadly matching income growth, hindering affordability. Croatia has adopted a National Plan for Housing Policy until 2030 and has already implemented some of the Plan's measures, including housing tax reforms, but further reforms are needed to improve the housing market and increase affordability. Effective and coordinated implementation of the Housing Policy Plan, particularly locally relevant measures to strengthen housing supply in high-demand areas and activate vacant dwellings, would improve affordable housing. Croatia also lacks a national-level monitoring framework for social housing, which is decentralised and managed at the local level. While local authorities are well placed to determine local social housing needs, a national monitoring framework would better capture housing challenges for vulnerable groups across the country and inform appropriate policy action for affordable and social housing.

(39) In view of the close interlinkages between the economies of euro-area Member States and their collective contribution to the functioning of the economic and monetary union, in 2026 the Council recommended that the euro-area Member States take action, including through their recovery and resilience plans, to implement the 2026 Recommendation on the economic policy of the euro area. For Croatia, the recommendation (1) helps implement the first, the second recommendation and the third recommendations on the euro area, recommendation (2) helps implement the fourth recommendation on the euro area, recommendation (3) helps implement the seventh, the ninth and the tenth recommendations on the euro area, recommendation (4) helps implement the seventh recommendation on the euro area and the recommendation (5) helps implement the fifth recommendation on the euro area.

HEREBY RECOMMENDS that Croatia take action in 2026 and 2027 to:

1. Take action to control net expenditure so that it respects the maximum growth rates recommended by the Council on 21 January 2025 given the material deviation recorded by 2025 and projected for 2026 by the Commission vis-à-vis the recommended net expenditure ceiling, while making use of the flexibility under the national escape clause activated by the Council. Reinforce overall defence and security spending and readiness, while ensuring debt sustainability and spending efficiency, as well as gradually adapting the budget to sustain structurally higher defence spending. Ensure that measures taken to mitigate the impact of the hike in energy prices resulting from the crisis are temporary, targeted at protecting vulnerable households or at addressing the needs of energy-intensive firms, preserve incentives for energy savings and that their fiscal cost is compatible with the commitments under the EU fiscal framework. Improve the efficiency of public expenditure by strengthening the role of regular spending reviews as integral part of the budgetary framework. Review the effectiveness of tax expenditures. Continue advancing the reform of recurrent property taxation by completing the necessary administrative infrastructure and introducing a value-based system.

2. Ensure continuity of reforms and investments implemented under the Recovery and Resilience Facility. Sustain implementation momentum under cohesion policy programmes, building, where appropriate, on the reallocation to strategic priorities and flexibilities agreed in the context of the mid-term review of the cohesion policy framework.

3. Promote the consolidation, collaboration and, where relevant, mergers of public research institutes and universities. Foster R&I investments, coordination and governance, while considering regional disparities. Continue improving access to diverse financing and deepen capital markets by further facilitating retail and institutional investor participation, expanding venture capital, addressing listing barriers, and strengthening corporate governance. Simplify regulation and reduce administrative burden through better coordination across government levels and digital tools integration, and streamline permitting to support the clean industrial transition. Merge local level public administration functions and/or municipalities and enhance human resource management. Further improve the efficiency of the justice system. Accelerate broadband deployment in underserved areas, particularly rural areas and islands.

4. Accelerate the deployment of renewable energy to lower wholesale electricity prices by upgrading electricity grids and investing in electricity storage. Advance the roll-out of smart meters and promote dynamic contracts. Streamline permitting and grid connection procedures for renewables and energy communities. Accelerate the implementation of energy efficiency measures and promote efficient and green solutions for heating and cooling. Promote sustainable urban transport, rail and the electrification of road transport. Phase out fossil fuel subsidies, particularly in the transport sector. Address the risk from natural hazards by improving governance, investing in climate resilience, and creating incentives for climate risk insurance. Further foster circular economy.

5. Reduce labour and skills shortages by removing obstacles to labour force participation, strengthening education at all levels, particularly for basic and STEM skills, and ensuring enough qualified teachers. Strengthen upskilling and reskilling and enhance work-based learning. Better target active labour market policies to vulnerable groups, and strengthen efforts to attract, develop and retain talent. Reduce poverty and income inequality by increasing the adequacy of social benefits while maintaining fiscal sustainability through better targeting. Improve access to formal home- and community-based long-term care. Balance the geographical distribution of health workers and facilities, invest in e-health, and strengthen prevention. Increase housing supply in high-demand areas and improve monitoring of affordable and social housing.

Done at Brussels,

For the Council
The president