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Recommendation for a

COUNCIL RECOMMENDATION

on the 2022 National Reform Programme of Croatia and delivering a Council opinion on the 2022 Convergence Programme of Croatia

{SWD(2022) 613 final} - {SWD(2022) 640 final}

Recommendation for a

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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 Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 9(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) 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,

Whereas:

(1) Regulation (EU) 2021/241 of the European Parliament and of the Council[3], which established the Recovery and Resilience Facility, entered into force on 19 February 2021. The Recovery and Resilience Facility provides financial support for the implementation of reforms and investment, entailing a fiscal impulse financed by the Union. It contributes to the economic recovery and to the implementation of sustainable and growth-enhancing reforms and investment, in particular to promote the green and digital transition, while strengthening the resilience and potential growth of the Member States' economies. It also helps strengthen sustainable public finances and boost growth and job creation in the medium and long term. The maximum financial contribution per Member State under the Recovery and Resilience Facility [was] updated on [XX] June 2022, in line with Article 11(2) of Regulation (EU) 2021/2411.

(2) On 24 November 2021, the Commission adopted the Annual Sustainable Growth Survey, marking the start of the 2022 European Semester for economic policy

[1] OJ L 209, 2.8.1997, p. 1.
[2] OJ L 306, 23.11.2011, p. 25.
[3] Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 stablishing the Recovery and Resilience Facility (OJ L 57, 18.2.2021, p. 17).

coordination. It took due account of the reaffirmed joint commitment of the Porto Social Summit of May 2021 to further implement the European Pillar of Social Rights, proclaimed by the European Parliament, the Council and the Commission on 17 November 2017. The European Council endorsed the priorities of the 2022 Annual Sustainable Growth Survey on 25 March 2022. On 24 November 2021, on the basis of Regulation (EU) No 1176/2011, the Commission also adopted the Alert Mechanism Report, in which it identified Croatia as one of the Member States for which an in-depth review[4] would be needed. On the same date, the Commission adopted the proposal for the 2022 Joint Employment Report analysing the implementation of the Employment Guidelines and the principles of the European Pillar of Social Rights, which was adopted by the Council on 14 March 2022.

(3) Russia´s invasion of Ukraine, in the wake of the global pandemic, has significantly altered the geopolitical and economic context. The impact of the invasion on Member States' economies has been felt for example through higher energy and food prices and weaker growth prospects. The higher energy prices weigh particularly on the most vulnerable households experiencing energy poverty. The EU is also seeing an unprecedented inflow of people fleeing Ukraine. In this context, on 4 March 2022, the Temporary Protection Directive was triggered[5] for the first time, granting displaced persons from Ukraine the right to legally stay in the EU, as well as access to education and training, labour market, healthcare, housing and social welfare.

(4) Taking account of the rapidly changing economic and geopolitical situation, the European Semester resumes its broad economic and employment policy coordination in 2022, while evolving in line with the implementation requirements of the Recovery and Resilience Facility as outlined in the 2022 Annual Sustainable Growth Survey. The implementation of the adopted recovery and resilience plans is essential for the delivery of the policy priorities under the European Semester, as the plans address all or a significant subset of the relevant country-specific recommendations issued in the 2019 and 2020 Semester cycles. The 2019 and 2020 country-specific recommendations remain equally relevant also for recovery and resilience plans revised, updated or amended in accordance with Articles 14, 18 and 21 of Regulation (EU) 2021/241, in addition to any country-specific recommendations issued up to the date of submission of the modified plan.

(5) The General Escape Clause has been active since March 2020[6]. In its Communication of 3 March 2021[7], the Commission set out its view that the decision on the deactivation or continued application of the general escape clause should be taken as an overall assessment of the state of the economy, with the level of economic activity in the EU or euro area compared to pre-crisis levels (end-2019) as a key quantitative criterion. Heightened uncertainty and strong downside risks to the economic outlook in the context of war in Europe, unprecedented energy price hikes and continued

[4] Regulation (EU) No1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances, OJ L 306, 23.11.2011, p. 25.

[5] Council Implementing Decision (EU) 2022/382 of 4 March 2022 establishing the existence of a mass influx of displaced persons from Ukraine within the meaning of Article 5 of Directive 2001/55/EC, and having the effect of introducing temporary protection, OJ L 71, 4.3.2022, p. 1.

[6] Communication from the Commission to the Council on the activation of the general escape clause of the Stability and Growth Pact, Brussels, 20.3.2020, COM(2020) 123 final.

[7] Communication from the Commission to the Council on one year since the outbreak of COVID-19: fiscal policy response, Brussels, 3.3.2021, COM(2021) 105 final.

supply chain disturbances warrant the extension of the general escape clause of the Stability and Growth Pact through 2023.

(6) Following the approach in the Council opinion of 18 June 2021 on the 2021 Convergence Programme, the fiscal stance is currently best measured as the change in primary expenditure (net of discretionary revenue measures), excluding COVID-19 crisis-related temporary emergency measures but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to medium-term potential growth[8]. Going beyond the overall fiscal stance, in order to assess whether national fiscal policy is prudent and its composition is conducive to a sustainable recovery consistent with the green and digital transitions, attention is also paid to the evolution of nationally-financed[9] primary current expenditure (net of discretionary revenue measures and excluding COVID-19 crisis-related temporary emergency measures) and investment.

(7) On 2 March 2022, the Commission adopted a Communication providing broad guidance for fiscal policy in 2023, aiming at supporting the preparation of Member States' Stability and Convergence Programmes and thereby strengthening policy coordination[10]. The Commission noted that, based on the macroeconomic outlook of the 2022 winter forecast, transitioning from an aggregate supportive fiscal stance in 2020-2022 to a broadly neutral aggregate fiscal stance would appear appropriate in 2023, while standing ready to react to the evolving economic situation. The Commission announced that the fiscal recommendations for 2023 should continue to differentiate across Member States and take into account possible cross-country spillovers. The Commission invited the Member States to reflect the guidance in their Stability and Convergence Programmes. The Commission committed to closely monitor the economic developments and adjust its policy guidance as needed and at the latest in its Semester spring package of late May 2022.

(8) With respect to the fiscal guidance provided on 2 March 2022, the fiscal recommendations for 2023 take into account the worsened economic outlook, the heightened uncertainty and further downside risks, and the higher inflation compared to the winter forecast. Against these considerations, the fiscal response has to expand public investment for the green and digital transition and energy security, and sustain the purchasing power of the most vulnerable households so as to cushion the impact of the energy price hike and help limit inflationary pressures from second round effects via targeted and temporary measures; fiscal policy has to remain agile so as to adjust to the rapidly evolving circumstances, and be differentiated across countries depending on their fiscal and economic situation, including as regards the exposure to the crisis and the inflow of displaced persons from Ukraine.

(9) On 14 May 2021, Croatia submitted its national recovery and resilience plan to the Commission, in accordance with Article 18(1) of Regulation (EU) 2021/241. Pursuant to Article 19 of Regulation (EU) 2021/241, the Commission assessed the relevance, effectiveness, efficiency and coherence of the recovery and resilience plan, in

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8 The estimates on the fiscal stance and its components in this recommendation are Commission estimates based on the assumptions underlying the Commission 2022 spring forecast. The Commission's estimates of medium-term potential growth do not include the positive impact of reforms that are part of the Recovery and Resilience Plan and that can boost potential growth.

9 Not financed by grants from the Recovery and Resilience Facility and other EU funds.

10 Communication from the Commission to the Council: Fiscal policy guidance for 2023, Brussels, 2.3.2022, COM(2022) 85 final.

accordance with the assessment guidelines of Annex V to that Regulation. On 20 July 2021, the Council adopted its Decision on the approval of the assessment of the recovery and resilience plan for Croatia[11]. The release of instalments is conditional on a decision by the Commission, taken in accordance with Article 24(5) of Regulation (EU) 2021/241, that Croatia has satisfactorily fulfilled the relevant milestones and targets set out in the Council Implementing Decision. Satisfactory fulfilment presupposes that the achievement of preceding milestones and targets has not been reversed.

(10) On 28 April 2022, Croatia submitted its 2022 National Reform Programme and, on 29 April 2022, its 2022 Convergence Programme, in line with Article 4 of Regulation (EC) No 1466/97. To take account of their interlinkages, the two programmes have been assessed together. In accordance with Article 27 of Regulation (EU) 2021/241, the 2022 National Reform Programme also reflects Croatia's bi-annual reporting on the progress made in achieving its recovery and resilience plan.

(11) The Commission published the 2022 country report for Croatia[12] on 23 May 2022. It assessed Croatia's progress in addressing the relevant country-specific recommendations adopted by the Council in 2019, 2020 and 2021, and took stock of Croatia's implementation of the recovery and resilience plan, building on the Recovery and Resilience Scoreboard. Based on this analysis, the country report identified gaps with respect to those challenges that are not addressed or only partially addressed by the recovery and resilience plan, as well as new and emerging challenges, including those emerging from Russia's invasion of Ukraine. It also assessed Croatia's progress in implementing the European Pillar of Social Rights and on achieving the EU headline targets on employment, skills and poverty reduction, as well as progress in achieving the UN's Sustainable Development Goals.

(12) The Commission carried out an in-depth review under Article 5 of Regulation (EU) No 1176/2011 for Croatia and published its results on 23 May 2022[13]. The Commission concluded that Croatia is no longer experiencing macroeconomic imbalances. In particular, important progress has been made in reducing private indebtedness and net external liabilities, while government debt remains high but has resumed the downward trajectory that delivered marked improvements before the pandemic.

(13) On 20 July 2020, the Council recommended Croatia to take in 2020 and 2021 all necessary measures, in line with the general escape clause, to effectively address the pandemic, sustain the economy and support the ensuing recovery. It also recommended Croatia to pursue, when economic conditions allow, fiscal policies aimed at achieving prudent medium-term fiscal positions and ensuring debt sustainability, while enhancing investment. In 2021, based on data validated by Eurostat, Croatia's general government deficit decreased from 7.3% of GDP in 2020 to 2.9% in 2021. The fiscal policy response by Croatia supported the economic recovery in 2021, while temporary emergency support measures declined from 3.3 % of GDP in 2020 to 2,1% in 2021. The measures taken by Croatia in 2021 have been in line with the Council Recommendation of 20 July 2020. The discretionary budgetary

[11] Council Implementing Decision of 6 July 2021 on the approval of the assessment of the recovery and resilience plan for Croatia (ST 10149 2021)
[12] SWD(2022) 613 final.
[13] SWD(2022) 633 final.

measures adopted by the government in 2020 and 2021 were mostly temporary or matched by offsetting measures. At the same time, some of the discretionary measures adopted by the government in 2021 were not temporary or matched by offsetting measures, mainly consisting of reduction of the personal and corporate income tax amounting in total to 0.5% of GDP. Based on data validated by Eurostat, general government debt stood at 79.8% of GDP in 2021.

(14) The macroeconomic scenario underpinning the budgetary projections in the 2022 Convergence Programme is cautious in 2022 and favourable thereafter. The government projects real GDP to grow by 3.0% in 2022 and 4.4% in 2023. By comparison, the Commission's 2022 spring forecast projects a higher real GDP growth of 3.4% in 2022 and a lower growth of 3.0% in 2023, with the difference mainly reflecting a lower expectation in 2022 by the Croatian authorities concerning growth in real household consumption. In its 2022 Convergence Programme, the Government expects that the headline deficit will slightly decrease to 2.8 % of GDP in 2022 and to 1.6% in 2023. The slight decrease in 2022 mainly reflects the growth in economic activity and the unwinding of most emergency measures. According to the Programme, the general government debt-to-GDP ratio is expected to decrease to 76.2% in 2022, and to decline to 71.7% in 2023. Based on policy measures known at the cut-off date of the forecast, the Commission 2022 spring forecast projects a government deficit for 2022 and 2023 of 2.3% of GDP and 1.8% respectively. This is lower than the deficit projected for 2022 and higher then the deficit projected for 2023 in the Convergence Programme, mainly due to a lower level of expenditure expected by the Commission in 2022 for gross fixed capital formation and other expenditure. Furthermore the Commission forecast entails somewhat lower level shift in both revenues and expenditures attributed to a difference in the inflation outlook. The Commission 2022 spring forecast projects a lower general government debt-to-GDP ratio, of 75.3% in 2022 and a higher level 73.1% in 2023.

Based on the Commission spring 2022 forecast, the medium-term (10-year average) potential output growth is estimated at 2.2 %. However, this estimate does not include the impact of the reforms that are part of the Recovery and Resilience Plan and can boost Croatia's potential growth.

(15) In 2022, the government phased out the majority of measures taken in response to the COVID-19 crisis, such that the temporary emergency support measures are projected to decline from 2.1% of GDP in 2021 to 0.4% in 2022. The government deficit in 2022 is impacted by the measures adopted to counter the economic and social impact of the increase in energy prices, which in the Commission spring 2022 forecast are estimated at 0.4% of GDP in 2022 and 0.2% of GDP in 2023.[14] These measures mainly consist of social transfers to poorer households, support for companies and cuts to indirect taxes on energy consumption. These measures are mostly temporary. However, in case energy prices remain elevated also in 2023, some of these measures could be continued. Some of these measures are not targeted, notably the across the board cuts on indirect taxes on energy. The government deficit is also impacted by the costs to offer temporary protection to displaced persons from Ukraine, which in the

14 The figures represent the level of annual budgetary costs of those measures taken since autumn 2021, including current revenue and expenditure as well as – where relevant – capital expenditure measures.

Commission 2022 spring forecast are projected at 0.1% of GDP in 2022 and 0.1% in 2023.[15]

(16) On 18 June 2021, the Council recommended that in 2022 Croatia[16] maintain a supportive fiscal stance, including the impulse provided by the Recovery and Resilience Facility, and preserve nationally financed investment. The Council also recommended Croatia to keep the growth of nationally financed current expenditure under control. It also recommended Croatia to pursue, when economic conditions allow, a fiscal policy aimed at achieving prudent medium-term fiscal positions and ensuring fiscal sustainability in the medium term, and at the same time, to enhance investment to boost growth potential.

(17) In 2022, based on the Commission's 2022 spring forecast and including the information incorporated in Croatia's 2022 Convergence Programme, the fiscal stance is projected to be supportive at -1.8% of GDP, as recommended by the Council.[17] Croatia plans to provide continued support to the recovery by making use of the Recovery and Resilience Facility to finance additional investment as recommended by the Council. The positive contribution to economic activity of expenditure financed by Recovery and Resilience Facility grants and other EU funds is projected to increase by 0.5 percentage points of GDP compared to 2021. Nationally-financed investment is projected to provide an expansionary contribution to the fiscal stance of 0.4 percentage points in 2022.[18] Therefore, Croatia plans to preserve nationally financed investment, as recommended by the Council. At the same time, the growth in nationally-financed primary current expenditure (net of new revenue measures) in 2022 is projected to provide an expansionary contribution of 1.0 percentage points to the overall fiscal stance. This significant expansionary contribution includes the additional impact of the measures to address the economic and social impact of the increase in energy prices (0.4% of GDP) as well as the costs to offer temporary protection to displaced persons from Ukraine (0.1% of GDP), while higher intermediate consumption expenditure, in part reflecting the increase in inflation, is also projected to contribute to the growth in net current expenditure. Therefore, on the basis of current Commission estimates, Croatia does not sufficiently keep under control the growth of nationally-financed current expenditure in 2022.

(18) In 2023, the fiscal stance is projected in the Commission 2022 spring forecast at -0.7% of GDP on a no-policy change assumption.[19] Croatia is projected to continue using the

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15 The total number of displaced persons from Ukraine to the EU is assumed to gradually reach 6 million by the end of 2022, and their geographical distribution is estimated based on the size of the existing diaspora, the relative population of the receiving Member State, and the actual distribution of displaced persons from Ukraine across the EU as of March 2022. For budgetary costs per person, estimates are based on the Euromod microsimulation model of the Commission's Joint Research Centre, taking into account both cash transfers people may be eligible for as well as in-kind benefits such as education and healthcare.

16 Council Recommendation of 18 June 2021 delivering a Council opinion on the 2021 Convergence Programme of Croatia, OJ C 304, 29.7.2021, p. 48.

17 A negative (positive) sign of the indicator corresponds to an excess (shortfall) of primary expenditure growth compared with medium-term economic growth, indicating an expansionary (contractionary) fiscal policy.

18 Other nationally-financed capital expenditure is projected to provide a slightly contractionary contribution of 0.1 percentage points of GDP.

19 A negative sign of the indicator corresponds to an excess of primary expenditure growth compared with medium-term economic growth, indicating an expansionary fiscal policy.

grants from the Recovery and Resilience Facility in 2023 to finance additional investment in support of the recovery. The positive contribution to economic activity of expenditure financed by Recovery and Resilience Facility grants and other EU funds is projected to increase by 0.5 percentage points compared to 2022. Nationally-financed investment is projected to provide a slightly expansionary contribution to the fiscal stance of 0.1 percentage points in 2023.[20] At the same time, the growth in nationally-financed primary current expenditure (net of new revenue measures) in 2023 is projected to provide a broadly neutral contribution of -0.2 percentage points to the overall fiscal stance. This includes the impact from the phasing out of some measures addressing the increased energy prices (0.2% of GDP). Therefore, the broadly neutral contribution of nationally-financed current expenditure relies partially on the phasing out of the measures to address the impact of the increase in energy prices as currently planned.

(19) In the 2022 Convergence Programme, the general government deficit is expected to gradually decline to 1.6% of GDP in 2024 and to 1.2% by 2025. Therefore, the general government deficit is planned to remain below 3% of GDP by 2025. According to the Programme, the general government debt-to-GDP ratio is expected to decrease by 2025, specifically with a decrease to 68.9% in 2024, and a decline to 66.9% in 2025. Based on the Commission's analysis, debt sustainability risks appear medium over the medium term.

(20) In accordance with Article 19(3), point (b), and Annex V, criterion 2.2, to Regulation (EU) 2021/241, the recovery and resilience plan includes an extensive set of mutually reinforcing reforms and investments to be implemented by 2026. These help address all or a significant subset of the economic and social challenges outlined in the country-specific recommendations addressed to Croatia by the Council in the European Semester in 2019 and 2020, in addition to any country-specific recommendations issued up to the date of adoption of the plan.

(21) In particular, the plan addresses the country-specific recommendations with reforms to reinforce the budgetary framework, active labour market policy measures and an education reform to improve access to education and the quality and labour-market relevance of education. The challenges faced by the Croatian healthcare system are addressed by measures to improve the efficiency, quality, accessibility, and financial sustainability, which was especially stricken by the COVID-19 pandemic. Furthermore, the plan addresses country-specific recommendations in those areas by advancing the decarbonisation of the energy sector, increasing overall energy efficiency, and focusing investments on sustainable transport and digital infrastructure and services. Moreover, the plan contains far-reaching measures to improve the efficiency of the public administration and justice system, to prevent, detect and correct corruption, to improve the business environment and support investment in and the policy relevance of research and innovation.

(22) The implementation of the recovery and resilience plan of Croatia is expected to contribute to making further progress on the green and digital transition. Measures supporting the climate objectives in Croatia account for 40.3% of the plan's total allocation, while measures supporting digital objectives account for 20.4% of the plan's total allocation. The fully-fledged implementation of the recovery and resilience

[20] Other nationally-financed capital expenditure is projected to provide a slightly contractionary contribution of 0.1 percentage points of GDP.

plan, in line with the relevant milestones and targets, will help Croatia swiftly recover from the fallout of the COVID-19 crisis, while strengthening its resilience. The systematic involvement of social partners and other relevant stakeholders remains important for the successful implementation of the recovery and resilience plan, as well as other economic and employment policies going beyond the plan, to ensure broad ownership of the overall policy agenda.

(23) Croatia has not yet submitted the Partnership Agreement and the other cohesion policy programming documents[21]. In line with Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021, Croatia shall take into account the relevant country-specific recommendations in the programming of the 2021-2027 cohesion policy funds. This is a prerequisite for improving the effectiveness and maximising the added value of the financial support to be received from cohesion policy funds, while promoting the coordination, complementarity and coherence between these funds and other Union instruments and funds. The successful implementation of the Recovery and Resilience Facility and cohesion policy programmes also depends on the removal of bottlenecks to investment to support the green and digital transition and balanced territorial development.

(24) In response to the mandate by the EU Heads of State or Government, as set out in the Versailles Declaration, the REPowerEU plan aims to phase out the European Union´s dependence on fossil fuel imports from Russia as soon as possible. For this purpose, the most suitable projects, investments and reforms at national, regional and EU level are being identified in dialogue with the Member States. These measures aim to reduce overall reliance on fossil fuels, and shift fossil fuel imports away from Russia.

(25) Croatia has committed to a phase-out of coal for electricity production by 2033. In 2020, Croatia reached a share of 28% of energy from renewable sources in gross final energy consumption, exceeding its target of 20%. Croatia needs to accelerate decarbonisation efforts, including in the industry, reduce energy import dependency from Russia, and take measures to foster integration in the single market. In 2021, imports of Russian gas accounted for 22% of total natural gas supply, whereas 57% was imported through the new Liquefied Natural Gas (LNG) terminal (operating since the beginning of 2021). Gas and oil represent 30.3% and 33.7% of the Croatian energy mix, respectively. Any new infrastructure and network investments related to gas are recommended to be future-proof where possible, in order to facilitate their long-term sustainability through future repurposing for sustainable fuels.

As regards developing renewable, secure and affordable energy, considerable potential remains in wind and solar energy, which represent around 2.1% of the energy mix (with shares of 13% and 1% of the total installed electricity-generation capacity, respectively), and in geothermal energy sources. Key aspects to improve the efficiency of the energy system, security of supply and market integration are: streamlining permit procedures for renewables, supporting the development of energy communities and frontloading investments in renewables, including by households and for small-scale systems.

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[21] Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, the Just Transition Fund and the European Maritime, Fisheries and Aquaculture Fund and financial rules for those and for the Asylum, Migration and Integration Fund, the Internal Security Fund and the Instrument for Financial Support for Border Management and Visa Policy.. OJ L 231, 30.6.2021, p. 159.

Further upgrades to electricity transmission and distribution grids will be required to support the green transition, while investments in electricity storage will be key to managing an energy system with a high share of renewables. Improvements are also necessary in the heating and cooling sector, most notably by transitioning from fossil-based district and individual heating systems to renewable energy sources directly or through electricity generation.

(26) As regards energy efficiency, measures are necessary to step-up building renovation of the building stock, the supply of energy-efficient housing, in particular social housing, and the replacement of gas and oil boilers with heat pumps and other more efficient and green solutions. In addition, more action is needed to reduce the oil dependence of Croatia's transport sector, particularly by increasing the use of public transport and further greening it, using intelligent transport systems, deploying electric and hydrogen charging stations and transportation more broadly, investing in mobility infrastructure and increasing the uptake of zero- and low-emission vehicles. Further increase in ambition for reducing greenhouse gas emissions and increasing renewable energy and energy efficiency will be needed to be in line with the 'Fit for 55' objective.

(27) While the acceleration of the transition towards climate neutrality and away from fossil fuels will create significant restructuring costs in several sectors, Croatia can make use of the Just Transition Mechanism in the context of the cohesion policy to alleviate the socio-economic impact of the transition in the most affected regions. In addition, Croatia can make use of the European Social Fund Plus to improve employment opportunities and strengthen social cohesion.

(28) In the light of the Commission's assessment, the Council has examined the 2022 Convergence Programme and its opinion[22] is reflected in recommendation (1) below.

(29) On 10 July 2020, the Croatian kuna was included in the European exchange rate mechanism II (ERM II) as a preparatory step towards adopting the euro. To preserve economic and financial stability and achieve a high degree of sustainable economic convergence, Croatian authorities have committed to implementing specific policy measures on anti-money laundering, the business environment, public-sector governance and the judiciary. Croatia's progress in fulfilling the necessary requirements to adopt the euro will be assessed in the 2022 Convergence Reports of the European Commission and the European Central Bank.

HEREBY RECOMMENDS that Croatia take action in 2022 and 2023 to:

1. In 2023, ensure that the growth of nationally-financed current expenditure is in line with an overall neutral policy stance, taking into account continued temporary and targeted support to households and firms most vulnerable to energy price hikes and to people fleeing Ukraine. Stand ready to adjust current spending to the evolving situation. Expand public investment for the green and digital transition and for energy security, including by making use of the RRF, RePowerEU and other EU funds. For the period beyond 2023, pursue a fiscal policy aimed at achieving prudent medium-term fiscal positions.

2. Proceed with the implementation of its recovery and resilience plan, in line with the milestones and targets included in the Council Implementing Decision of 20 July

[22] Under Article 9(2) of Council Regulation (EC) No 1466/97.

2021. Submit the 2021-2027 cohesion policy programming documents with a view to finalising these negotiations with the Commission and starting their implementation.

3. Diversify fossil fuel imports and reduce overall reliance on fossil fuels. Accelerate the deployment of renewables, focussing in particular on wind, solar and geothermal sources, including through small-scale renewable energy production and developing energy communities, mainly by streamlining procedures for administrative authorisation and permits. Further upgrade electricity transmission and distribution grids and invest in electricity storage. Step-up action to reduce energy demand by improving energy efficiency, mainly in residential buildings, and to reduce dependence on fossil fuels in the heating and transport sectors.

Done at Brussels,

For the Council
The President