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In the published version of this decision, some information has been omitted, pursuant to articles 30 and 31 of Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus […]		PUBLIC VERSION This document is made available for information purposes only.

Subject: State Aid SA.58248 (2020/NN) – Croatia - Restructuring of Đuro Đaković

Excellency,

The European Commission ("the Commission") wishes to inform the Republic of Croatia ("Croatia") that, having examined the information supplied by your authorities on the State aid referred to above, it has decided not to raise any objections, as it is compatible with the internal market pursuant to Article 107(3)(c) of the Treaty on the Functioning of the European Union ("TFEU").

The Commission has based its decision on the following considerations.

1. PROCEDURE

(1) On 8 May 2020, the Commission decided to raise no objections on a State aid in the form of a loan of HRK 300 million (approximately EUR 40.31 million) for the rescue of the group controlled by Đuro Đaković Grupa d.d. ("Đuro Đaković" or "the beneficiary") ("the rescue aid decision")[1] on the ground that the rescue aid met the conditions for compatibility with the internal market laid down in Guidelines on State

[1] Commission Decision in case SA.56216 (2020/NN) – Rescue aid to Đuro Đaković, OJ C 430 11.12.2020, p. 1.

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aid for rescuing and restructuring non-financial undertakings in difficulty[2] ("R&R Guidelines").

(2) The rescue aid decision noted (recital 26) that on 24 January 2020 the Croatian authorities had put into effect the State guarantee for half of the rescue loan amount pledged by the Government Decision of 16 January 2020 (“the Government decision”), before the notification and without the Commission's prior approval.

(3) Croatia was not expecting that Đuro Đaković would reimburse the loan within six months after the disbursement of the first instalment, that is, by 24 July 2020, and committed that, within such six months, if the rescue aid was not repaid, it would submit to the Commission a restructuring plan for Đuro Đaković[3].

(4) On 30 July 2020, the Croatian authorities submitted to the Commission a first restructuring plan. After the beneficiary completed the search for a private investor announced in the first restructuring plan, the private investor and Croatia have prepared a revised restructuring plan based on the business plan of the investor. By a letter of 20 September 2020 the Commission informed Croatia that the restructuring aid was unlawful, as it was put into effect without a prior Commission approval (Article 1 (f) of the Procedural Regulation[4]), without prejudice to the Commission’s assessment of the restructuring plan once the pending elements had been defined and the final plan notified. On 30 June 2021, Croatia submitted to the Commission the final restructuring plan of Đuro Đaković, supported with State aid in the total amount of HRK 430.6 million (approximately EUR 57.4 million).

(5) The Commission requested additional information, which the Croatian authorities provided in written or oral exchanges on 23 July 2021, 30 August 2021, 2 September 2021, 3 September 2021, 17 September 2021, 20 September 2021, 17 November 2021, 23 November 2021 and 8 December 2021.

(6) The Croatian authorities agreed exceptionally to waive their rights deriving from Article 342 TFEU in conjunction with Article 3 of Regulation 1/1958[5] and to have this decision adopted and notified pursuant to Article 297 TFEU in English.

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2 Communication from the Commission – Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty, OJ C 249, 31.7.2014, p. 1.

3 Rescue aid decision, recital 12.

4 Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union, OJ L 248, 24.9.2015, p. 9.

5 Council Regulation No 1 of 15 April 1958 determining the languages to be used by the European Economic Community, OJ 17, 6.10.1958, p. 385.

2. DESCRIPTION OF THE AID

2.1. The beneficiary

(7) As explained in the rescue aid decision (recital 2), Đuro Đaković is a metal mechanical engineering group located in Brod-Posavina County (Pannonian Croatia region, one of the four NUTS 2 Regions of Eastern Croatia since 2021), which manufactures products both for civil and military use. Đuro Đaković was first established in 1921 and has since undergone changes in ownership and structure. The present undertaking was established on 31 January 1991 with the Croatian Development Fund, the Croatian Railway Company d.o.o. and the Đuro Đaković Complex as shareholders. On 26 October 1993, Đuro Đaković become a joint stock company.

Đuro Đaković 's ownership structure

(8) The beneficiary is a diversified industrial group listed on the Zagreb stock exchange. The share capital of the beneficiary is HRK 203.064.600 (EUR 27 million) paid in full and allocated as 10.153.230 shares, with nominal value of HRK 20 (EUR 2.7) per share. Since its establishment, when the beneficiary was 100% controlled by the Croatian State, the shareholding has changed with a progressive reduction of the participation of the State in the share capital of the company. At the time of the rescue aid decision (recital 2 of the rescue aid decision), the Croatian State held 28.82% of the shares, including 6.5% through the Croatian Pension Fund, while two private entrepreneurs owned respectively 17.71% and 8.71% of the share capital and small shareholders the remainder (35.59%), with no single shareholder having more than 1% of it.

(9) As described in recital 32 of the rescue aid decision, Đuro Đaković is a group in itself, which is not part of a larger business group, and the financial difficulties at issue extend to the whole perimeter of the group, including its subsidiaries (mentioned in Table 2). Each Đuro Đaković share is an ordinary share registered in the same class, which gives their holders the right to participate in the company's management, the right to dividends and the right to the corresponding portion of the residual assets after liquidation or bankruptcy. All the shares are freely transferable and have no restrictions on voting rights as per the Articles of Association. Currently no shareholder exercises sole or joint control over Đuro Đaković. Until 2017 the State was the majority shareholder with 50.66% of the share capital. In 2018, the State shareholding was reduced to 37.86% of the share capital. Following the sale of shares to the investment consortium DD Acquisition ("DD Acquisition" or "the investor", described in recital (12) in more details) by the two private persons who were the largest shareholders with the State in November 2020, the major shareholders remain the Croatian State (with direct and indirect holding of 26.4%),

along with the new investor DD Acquisition (18.9 %) and another independent private undertaking (8.7%) not linked to either of the major shareholders, while the remaining shares are widely dispersed, being each shareholder below 1%. Since November 2020, the three largest shareholders together have a stake of 54% but they have no agreement to vote together and the absence or opposition of any one of the shareholders can be overcome by the remaining ones. Adoption of the most important decisions, such as on the business plan or the budget, require simple majority (50%) in the General Assembly, while 75% qualified majority is required only for certain exceptional decisions, such as increase or reduction of the share capital or pre-emption rights. Therefore, at least since the time of the rescue aid decision, the ownership structure is such that none of the shareholders can be described as having sole or joint control of Đuro Đaković. Table 1 shows the number and proportion of shares held after November 2020.[6]

'Table 1: Shareholders' structure of Đuro Đaković on 28 February 2021

No.	Shareholder	Number of shares (in thousands	Share capital (in thousands HRK)	% of ownership
	DD ACQUISITION A.S.	1.917	38.334	18.9
	CERP / REPUBLIC OF CROATIA	1.199	23.977	11.8
	PRIVATE UNDERTAKING	884	17.672	8.7
	HPB D.D. / REPUBLIC OF CROATIA	822	16.435	8.1
	CERP / HZMO /REPUBLIC OF CROATIA	660	13.200	6.5
	OTHERS	4.672	93.427	46
	Total	**10.152**	**203.045**	**100**

(10) According to the Articles of Association, the General Assembly appoints the Supervisory Board, which has seven members. The shareholders have agreed on who sits on that Supervisory Board: at present, it is composed of three members appointed by the State, two members appointed by the previous main private shareholder, one member appointed by the pension funds and one member representing the employees. Although the State currently has the right to appoint three out of the seven members of the Supervisory Board, and DD Acquisition has the right to appoint two members, this does not confer sole or joint control to them because the strategic decisions are reserved for the General Assembly.

[6] Đuro Đaković owns 46,855 of its own shares, nominal value of HRK 937,100, which accounts for 0.46 % of total shares issued.

(11) The Government's decision to support the rescue and restructuring of the beneficiary is subject to the condition of finding a strategic investor to recapitalise and restructure Đuro Đaković. The Czech investor DD Acquisition a.s. ("DD Acquisition" or "the investor") has been chosen as the most suitable bidder to enter into the capital of Đuro Đaković. In November 2020, as mentioned (recital (9)), DD Acquisition has thus acquired a minority share of over 18% from previous shareholders and is the largest shareholder after the State.

(12) In particular, DD Acquisition was established on 11 November 2020 to represent a consortium of investors interested in acquiring shareholding in Đuro Đaković. The members of the consortium are the following companies:

- CE Industries a.s. with the business seat in Praha, Czech Republic, with an ultimate owner Mr. Jaroslav Strnad and with shareholding of […] %.

- PROMET GROUP a.s. with the business seat in Ostrava, Czech Republic, with an ultimate owner Mr. René Matera and with shareholding of […] %.

- CZECHOSLOVAK GROUP a.s. with the business seat in Praha, Czech Republic, with ultimate owner Mr. Michal Strnad, with shareholding of […] %.

(13) The members of DD Acquisition consortium employ all together over 14.000 employees, manage more than 100 companies predominantly based in Europe and have more than EUR 1.7 billion aggregated revenues. The consortium members operate in segments of automotive, defence, aerospace, railway, engineering, recycling, facility & services, metallurgy and machinery. Some of the companies and brands controlled are Tatra Trucks, Excalibur Army, Eldis, Retia, Dako - CZ, Vítkovická Doprava, Vítkovické železniční opravny, Advance Energo, Tawesco and Promet Czech.

Đuro Đaković's structure

(14) Đuro Đaković is a parent company with four subsidiaries in which it holds more than 50% of share capital:

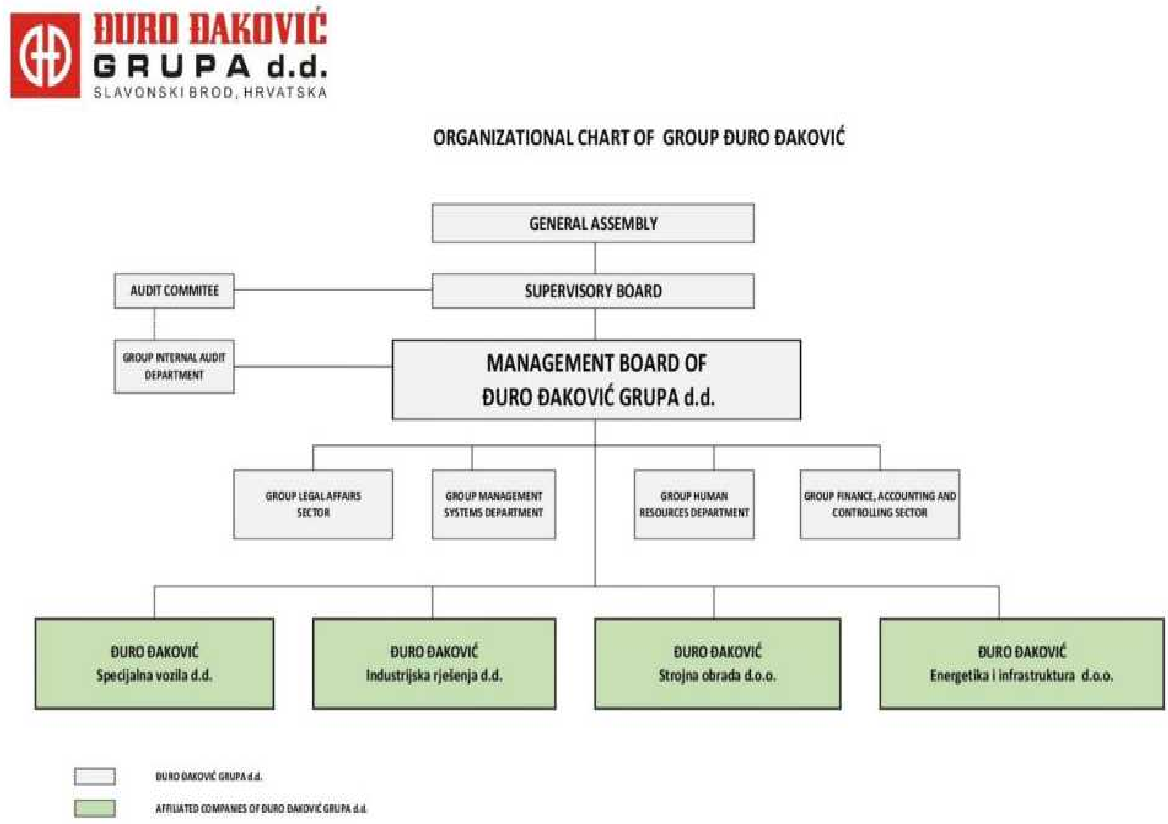
1. Đuro Đaković Specijalna vozila d.d. (ownership share: 99.84%);

2. Đuro Đaković Industrijska rješenja d.d. (ownership share: 99.51%);

3. Đuro Đaković Strojna obrada d.o.o. (ownership share: 100%);

4. Đuro Đaković Energetika i infrastruktura d.o.o. (ownership share: 97.55%).

Table 2: Đuro Đaković's structure



Source: ĐĐG

Source: Croatian authorities

Đuro Đaković's employees

(15) The total number of employees as of 31 December 2020 was 733. Table 3 shows the evolution of the number of employees since 2018.

Table 3: Number of employees of the beneficiary

Company	2018	2019	2020	Difference 2018 to 2019	Difference 2019 to 2020

Đuro Đaković group	23	21	14	*-2*	*-7*
Total	**992**	**794**	**733**	***-198***	***-61***

Source: Croatian authorities

Đuro Đaković's business activities and market position per segment

(16) Đuro Đaković operates in the following main segments: defence, railway, machining, industrial solutions and energy & infrastructure. Currently, the production focuses on special purpose freight wagons, primarily tailored to the specific requirements of customers and end users. Đuro Đaković mostly acts as an original equipment manufacturer and sells its products to the final customers.

(17) Although Đuro Đaković manufactures rolling stock, including locomotives, the production of this segment was close to discontinuation in 2013, when the beneficiary did not deliver a single freight wagon to the market. The production and sale of freight wagons now accounts for more 70% of total consolidated revenues. The key customers are leasing companies (GATX, Ermewa, VTG AG), which lease the wagons to providers of freight transport services. Total production of wagons recorded high growth rates, reaching 425 freight wagons delivered in 2018. This development of the rolling stock manufacturing - that had nearly come to a halt in 2013 - was based upon target positioning in specialized freight wagons, i.e. "Shimmns"[7] type, and entailed many start-up and one-time costs, including acquisition of licenses.

(18) Đuro Đaković's market share in the EU market for rail freight wagons is very small (3-4%), with other competitors having stronger positions, namely: Greenbrier Europe (around 30%), Tatravagonka (around 30%) and Transwagon (around 10%), Nymwag, Vako and Gokrail (around 20% altogether). Croatia puts forward that despite the production plans for the upcoming years, the market share of the beneficiary in the sector of new freight wagon production will not vary significantly, as the market is growing.

(19) As for the beneficiary's market shares in the segments of machinery, energy and infrastructure, which account for less than 20% of the beneficiary's sales revenues, Đuro Đaković plays an insignificant role in the EU market.

(20) As a result of restructuring, Đuro Đaković will refocus on its core business in the railway segment, where the freight wagons production will be integrated in the future with a repair and maintenance workshop, the long-established defence segments, as well as in machining.

[7] This is a covered freight wagon for transport of various goods.

(21) The military production is the smallest business of the group, with approximately 8.5% share in the revenues for the financial year 2020. Croatia explains that the development of new products in the defence sector requires high cost of research and development, and long development periods with uncertain returns. Therefore, Đuro Đaković now focuses on producing spare parts, components and servicing to reduce risks. The main customer is the Croatian Ministry of Defence, with more than 80% of expected revenues being related to repair and maintenance of armoury vehicles and sales of spare parts.

(22) Croatia informs that currently there is no order book for military production, although Đuro Đaković is a sole national provider in this sector on the Croatian market, in particular, as it supplies the Croatian Ministry of Defence with final products and/or servicing. For the future, Croatia will separate the military and civil productions with the defence part being put into an entity currently called "DD Defence".

Consequences of Đuro Đaković's potential market exit

(23) Croatia submits that Đuro Đaković has its headquarters and its manufacturing facilities in Slavonski Brod, a centre of Brod-Posavina County, which is eligible for assistance under Art. 107(3)(a) TFEU, as part of the NUTS 2 region Panonska Hrvatska (HR02) (previously, until 31 December 2020[8]: Kontinental Hrvatska or Continental Croatia (HR04), as per the NUTS Eurostat classification)[9]. The Kontinental Hrvatska region suffers from higher unemployment and larger emigration compared to the other Member States of the European Union ("EU-27"), with an unemployment rate persistently higher than the EU-27 since at least 2016. In particular, based on Eurostat available data (Table 4), which, however, still include Zagreb (since 2021 measured on its own, as capital region, HR05), unemployment rates in Continental Croatia (HR04) in 2016, 2017, 2018 and 2020 are respectively 12.6%, 11.4%, 8.0% and 7.5%, while the corresponding EU average unemployment rates are 9.1%, 8.1%, 7.2% and 7.1%[10]; only in 2019 the unemployment rates in the Continental Croatia region and the EU average aligned due to, as claimed by Croatia, (i) inclusion in the survey of the capital region of Zagreb (no longer measured in the NUTS 2 region of Panonska Hrvatska), which has the highest employment rate in Croatia, and (ii) increased emigration of work force to other Member States. Indeed, as Table 4 shows, unemployment data for Continental Croatia do not reflect the labour market conditions of the area of Brod-Posavina (a NUTS 3 region, HR24), where the

[8] See also Commission Decision of 23 November 2021 in SA.64581 (2021/N) - Croatia – Regional aid map for Croatia (2022-2027), available at: https://ec.europa.eu/competition/state_aid/cases1/202149/SA_64581_E0E65C7D-0000-C060-BE79-930CFDA9A8D0_52_1.pdf

[9] Background - NUTS - Nomenclature of territorial units for statistics - Eurostat (europa.eu).

[10] https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Labour_market_statistics_at_regional_level#Unemployment.

beneficiary is located[11]. As for the correlation between unemployment and depopulation, in addition to statistics submitted by Croatia[12], the Commission Staff Working Document, Country Report Croatia 2020, confirms that: "[…] *in 2018, unemployment rate fell to 8.4%, the lowest recorded level […] employment and labour market participation rates remain low, well below the EU average. […] There is also a high correlation between labour market outcomes and demographic change. Although the population has decreased across the country since 2010, poorer regions, especially in eastern Croatia, have experienced much higher rates of decline driven by outmigration and ageing*".[13] Moreover, the NUTS 2 region of Panonska Hrvatska (HR02), of which Brod-Posavina currently forms part, is included in the regional aid map for Croatia in accordance with Article 107(3)(a) TFEU, for the period 2022-2027, as one of the most disadvantaged regions of the EU in terms of gross domestic product per capita[14] and, thus, is eligible for regional aid[15].

Table 4: Unemployment rates

Reference year	**HR24 - Brod-Posavina**	**HR04 – Continental Croatia**	**Croatia**	**EU-27**
2016	27.1%	12.6%	16.9%	9.1%
2017	22.4%	11.4%	13.9%	8.1%
2018	19.9%	8%	11.1%	7.2%
2019	15.7%	6.7%	9.1%	6.7%
2020	14.6%	7.5%	7.5%	7.1%

[11] See also the Commission Staff Working Document, Country Report Croatia 2020, Accompanying the document Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank and the Eurogroup, 2020 European Semester: Assessment of progress on structural reforms, prevention and correction of macroeconomic imbalances, and results of in-depth reviews under Regulation (EU) No 1176/2011 (COM(2020) 150 final), https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1584545612721&uri=CELEX%3A52020SC0510.

[12] Base on statics provided by Croatia, the number of school-age children in the Brod-Posavina County decreased significantly in both elementary and high school. The number of children in elementary school decreased from 17.538 to 11.469 in the period 2005-2018, while, at the same time, number of children in high school decreased from 7.297 to 5.055.

[13] Commission Staff Working Document, Country Report Croatia 2020, quoted at footnote 13.

[14] See footnote 8.

[15] Decision of the European Commission of 23 November 2021 in case SA.64581 (2021/N) – Croatia Regional aid map for Croatia (1 January 2022 – 31 December 2027), not published yet, in which, given the region's gross domestic product per capita of 41.58% of the EU-27 average, the Commission accepted a maximum aid intensity of 50% for large enterprises in Panonska Hrvatska (HR02).

Source: Eurostat

(24) Croatia also explains that Panonska Hrvatska (HR02) is a diversified area with the Eastern part, including Brod-Posavina County (HR24), where Đuro Đaković is located, that has the highest unemployment rate in Croatia, with deep structural causes due to lack of industrial structures that would keep employment and reduce high emigration rates from this region in the last decade. In particular, the region of Slavonia, including Slavonski Brod, suffered from a large inhabitant emigration trend ever since Croatian joined the European Union and is currently depopulating, mainly as a consequence of the lack of job vacancies and narrow labour market[16]. Moreover, Đuro Đaković actively participates in developing a knowledgeable and skilful workforce, starting from high school and university students educated at the Mechanical Engineering Faculty in Đuro Đaković's neighbourhood and its production facilities in Slavonski Brod and Eastern Croatia. All these activities facilitate retention of the existing work force, not only those currently employed, but also attracting new workforce currently occupied elsewhere, to make sure that that the important technical knowledge and expertise is sustained. The Croatian authorities add that the COVID-19 pandemic situation has put additional pressure on the unemployment rate in the region, so that the gap with the EU-27 average is expected to widen. Therefore, since Đuro Đaković is one of the most important and largest employers in the region, its bankruptcy would cause losses of high end jobs in a structurally weak region with persistently high unemployment.

(25) Moreover, according to Croatia, the failure of Đuro Đaković's would likely cause serious social hardship, having a serious impact on the labour force, suppliers and customer chain, as well as on families dependent upon operations of Đuro Đaković. Finally, the supply in terms of defence and railway output would also be immediately disrupted, as Đuro Đaković is the sole national provider in these sectors on the Croatian relevant markets. In terms of defence, as the beneficiary provides service and maintenance, as well as components for the Patria and Kongsberg vehicles to the Ministry of Defence (recital (22)), in case of exit of Đuro Đaković from the market, the national defence needs would face an immediate risk of losing a supplier, which is difficult to replace, given the sensitivity and security clearance of supplies to national defence.

2.2. Causes of Đuro Đaković's difficulties and past financial performance

Operational difficulties due to changes in the production activity

(26) According to the Croatian authorities, the difficulties of Đuro Đaković have been mainly caused by several factors. First, in the early 1990s

[16] Commission Staff Working Document, Country Report Croatia 2020, quoted above.

Đuro Đaković changed its focus from the manufacture of locomotives and wagons to a defence segment, mainly being a supplier of the Croatian army. In particular, Đuro Đaković supplied the Croatian Ministry of Defence with military vehicles like the Patria AMV 8x8 modular wheeled vehicle or the M-84 tank. Đuro Đaković was then active for a prolonged period of time in the defence segment in close relation with the Croatian Ministry of Defence, which it served with repair and maintenance of armoury vehicles and sales of spare parts. This prevented the company from developing a culture focused on efficiency and profitability along the whole structure of the supply chain.

(27) After 2000, the beneficiary continued to focus its activity on the military segment and was manufacturing the Patria Armoured Modular Vehicle. The freight wagon manufacturing relied solely on a simple wagon type – "Faccns". During the financial crisis 2008-2009 and the recession afterwards, Đuro Đaković sold its profitable segments, while it simultaneously started accumulating debt on the balance sheet.

(28) After the military production programme (described in recital (25)) ended around 2014, the beneficiary started a much-needed substantive transformation, given its earlier strong dependence on the military segment. It thus started the production of more complex freight wagons, with partially own development and prototypes. However, the beneficiary was not organisationally or technically ready for this move. The beneficiary lacked the technical know-how to build those wagons, which resulted in delays, cost overruns and penalties for late delivery. According to Croatia, the sales prices of wagons, which the beneficiary's transport segment currently has in the production portfolio, are undervalued in comparison with market prices and current trends in the EU markets. The sale pricing process is not optimally set and, at the same time, the data to determine the complete cost price of production of the railcars are of insufficient detail and quality. Even without the other production weaknesses described below, the current wagon sales prices are perceived as an additional reason for the beneficiary's losses.

(29) Further problems resulted from the lack of proficiency in managing the supply chain (e.g. proper hedging of steel price, which is the main input cost) and commercial activity. In addition, Đuro Đaković has faced high interest expenses as interest rates in Croatia are around 2.25 percentage points higher than interest rates for competitors in the Eurozone. The prolonged period of liquidity problems and associated risks were incorporated in the purchasing prices for a longer period, as the suppliers reflect those risks in their prices and in their pressure for advance payments. Those circumstances hampered Đuro Đaković's ability to emerge from the financial downturn.

(30) As explained in the rescue aid decision (recitals 6-7), the commercial banks decided to stop their financing and the production of both wagons and parts stopped. In turn, key suppliers cancelled contracts or requested secured or bank guaranteed payment, which Đuro Đaković

was no longer able to provide. After exhaustion of own reserves, wages to workers were delayed, bank accounts were frozen and production eventually ceased by January 2020. The Croatian authorities submitted that, in these circumstances, without the rescue aid, the beneficiary would not have survived beyond one month.

Financial performance

(31) Over the last five years, Đuro Đaković's operational and financial situation has significantly deteriorated. Its operating profit is insufficient to cover net financial costs and depreciation, value adjustments and provisions, which has resulted in net operating losses in the years 2014 to 2018. In July 2019, Đuro Đaković qualified as an undertaking in difficulty within the meaning of the R&R Guidelines as confirmed in recital 30 of the rescue aid decision.

(32) A mismanagement of working capital caused liquidity problems. The solvency ratios of the beneficiary are significantly below larger competitors' and market levels. Currently, the beneficiary's liquidity position is very weak. The net working capital is lower than its peer group. Đuro Đaković has a limited access to external funding due to its high level of indebtedness. Therefore, it has been financing its operations largely through its suppliers by extending payment periods. After the approval of the rescue aid, the indebtedness increased even more. In such a situation, suppliers could refuse to deal with the beneficiary with consequent risks to production continuity.

(33) In 2019, Đuro Đaković's accumulated losses amounted to HRK 259 019 947 (EUR 35 million). As of 31 December 2019, Đuro Đaković's debt was more than sixteen times its capital.

(34) In 2020, Đuro Đaković continued to be an undertaking in difficulty showing the debt to equity ratio […] on 31 December 2020 and EBITDA interest coverage ratio […] on 31 December 2020. Đuro Đaković ended the year 2020 with a total loss of HRK […] million (EUR […] million). This result was however significantly less than the year before, when the loss exceeded HRK […] million (EUR […] million). In 2020, the total consolidated revenues of the Đuro Đaković amounted to HRK […] million (EUR […]million), which is HRK […] million (EUR […]million), or 40.08% more than in 2019, while total expenses grew much more slowly, by 1.75 percent, to HRK […] million (EUR […] million). The operating revenues in 2020 amounted to HRK […] million (EUR […] million), which is an annual increase of 39.62%, or HRK […] million (EUR […] million). The beneficiary had a negative operating result, loss before financial income and expenses (EBIT), as well as total operating loss, but in 2020 EBITDA was positive and amounted to HRK […] million (EUR […] million).

(35) In 2021, Đuro Đaković's financial situation remains delicate, as according to the quarterly reporting for the first quarter there is still a loss of more than half of the share capital with negative equity of HRK […] million (EUR […] million). Without the operational financing, the

beneficiary is very unlikely to undertake new large projects (mainly in the railway segment), which will start impacting its profitability and liquidity immediately. The cash flow projection shows that the beneficiary is not able to finance its operations. To conclude, in spite of the rescue aid, the beneficiary is still in difficulty. Moreover, it continues to incur financial losses and generate negative cash flows even in 2021. The consolidated loss (at the level of profit before tax) for the first 8 months of 2021 totalled HRK […] million (EUR […] million). The beneficiary foresees a negative free cash-flow for the year 2021 totalling HRK […] million (EUR […] million), which implies the need for urgent liquidity support not to risk a default.

Rescue aid

(36) Croatia reports that Đuro Đaković used the State guarantee approved by the rescue aid decision to obtain a loan from Hrvatska poštanska banka ("HPB") in the amount of HRK 150 million (EUR 20 million) with an interest rate of 4.3%, variable with a reference to the national inter-banking rate. The funds were used to repay due payments towards suppliers and banks, as well as salaries. The withdrawals of funds were monitored by KPMG Croatia.

(37) The other part of the approved rescue aid was used to obtain a loan from the Croatian Bank for Reconstruction and Development (HBOR) in the middle of 2020. HBOR provided an additional loan of HRK 60 million (EUR 8 million) which was used for operational financing of freight wagon production.

(38) Croatia submits that Đuro Đaković has not previously received any rescue aid, other than the one approved by the Commission in the rescue aid decision, nor restructuring aid.

2.3. The restructuring plan

(39) The duration of the restructuring plan presented by Croatia started running in 2020 and will run until 2024 with the aim of Đuro Đaković returning to its long-term viability while providing an appropriate return on capital.

The recapitalisation transaction

(40) The current shareholding structure of the beneficiary will be impacted through the process and sequence of individual steps, starting with the debt-to-equity swap at the level of Đuro Đaković d.d. (recital (56)), offsetting of accumulated losses against the share capital and closing with the capital injections by the new investor DD Acquisition. The planned capital contribution by the State will thus be recognised as equity.

(41) After the recapitalisation transaction, the shareholder structure of Đuro Đaković Grupa d.d. will change with the new investor becoming the majority shareholder and the State the second largest shareholder. The

recapitalisation involves the conversion into equity of the State-guaranteed loans of HRK […] million (around EUR […] million) out of which HRK 300 million (around EUR 40 million) were provided by Croatia to the beneficiary as rescue aid. The recapitalisation will be done in two instalments as shown in Table 5. As a part of the "1st Recapitalisation", the share capital will be reduced to proportionally offset the beneficiary's accumulated losses and, thus, a share reduction will be carried out. Afterwards, still as part of the "1st Recapitalisation"), Croatia will convert into equity state-guaranteed loans and new shares will be issued with a corresponding change in the shareholders' equity position. Following that, in a second phase the investor will inject new capital into Đuro Đaković Grupa d.d. ("2nd Recapitalisation) for a total amount of HRK 227.0 million (around EUR 30.3 million), and new shares will be issued with a corresponding change in the shareholders' equity position. The structure of the shareholding at the end of the entire recapitalisation transaction will change with the new investor becoming the majority shareholder and the State the second largest shareholder (Table 5 and explained in more details in recitals (61)-(63)).

Table 5: Shareholder structure in % at the end of the transaction

Đuro Đaković Grupa d.d.	**1st Recapitalisation**	**2nd Recapitalisation**
HR State	**[…]%**	**[…]%**
DD Acquisition	**[…]%**	**[…]%**
Others	[…]%	[…]%
TOTAL	100.00%	100.00%

Restructuring measures

(42) Đuro Đaković's restructuring plan provides for financial and operational restructuring. In particular, the plan emphasises that the customers are expected to support the restructuring process of the beneficiary. According to the Croatian authorities, the customers have continued to express their support for Đuro Đaković over the past years by awarding to Đuro Đaković new contracts for the wagon, defence and machining segment, including new orders made in the past year.

Operational restructuring

(43) On the operational side, the main goal of the plan is for the beneficiary to discontinue operations that do not provide for the comparative advantage. The beneficiary will focus on its core business to make operational improvements and undertake cost savings, which will improve its profitability level.

(44) The initiatives foreseen by the plan aim to simplify the group's operational footprint and to improve its profitability. This involves an optimisation of the production process and an improvement in

production effectiveness and productivity, sales processes and purchasing improvements, customer services improvements, reduction in transportation costs and reduction in general overheads. In addition, a corporate reorganisation, as well as an introduction of measures to reduce variable and fixed cost and capital employed will strengthen the competitive platform for the core business, namely the freight wagon industry.

(45) The operational restructuring initiatives comprise the following: i) the realignment of strategy and organisational structure, ii) a simplification and rationalisation of operational footprint, iii) operational cost savings, (iv) re-gaining trust of customers and suppliers, and v) utilising added value of the new investor DD Acquisition in all aspects, not only the cash and non-cash capital contributions, but also potential synergies, experience, market knowledge and bargaining power. Under the restructuring plan, the new investor is to sign an agreement with the beneficiary for the production and delivery to a known customer of 100 intermodal (container) wagons, which are expected to be manufactured and supplied during the restructuring period.

(46) These actions are projected to significantly improve the profitability and sustainability of the beneficiary, once all of them have been implemented, namely by the end of 2023. On top of the sustainable long-term improvements, additional one-off effects in the form of working capital improvement are expected.

(47) Improvements in purchasing are expected given that the beneficiary will now be able to select the best price offered and no longer the one with the longest payment terms, as it was the case in the past. Furthermore, wagon sales prices are agreed at one point of time and delivered over the following months and even years. According to the plan, fixing the pricing conditions for the key materials is of utmost importance for maintaining the desired profitability. The implementation of the new sales strategy has already started in mid-2021 with the investor nominating its representative to the Management Board of the beneficiary and introducing comprehensive operational measures (including a so-called “100 days programme”). The new major sales effort will start with the capital contribution of technical documentation to new wagon types that the investor intends to transfer to the beneficiary once the decision authorising the restructuring plan has been adopted.

(48) The production organisation is becoming another area of improvement, as the planning is no longer hugely influenced by lack of liquidity. Optimised use of resources, downtime and reduction in labour costs should bring down the production unit cost. Introduction of lean management principles in production offer is considered another major opportunity to reduce unit cost and contribute not only to overall increase of profitability, but also to increase Đuro Đaković’s competitiveness to win new projects.

Financial restructuring

(49) According to Croatia, the financial restructuring will primarily address the high level of debt. The over-indebtedness and level of interest rates Đuro Đaković has been paying resulted in high interest expenses. The aim is that with the decrease of the debt level this expense will come down. The interest rates have in the recent years been at significantly higher level than in the rest of EU, making Đuro Đaković less or non-competitive from this angle. Therefore, reducing over-indebtedness is a central part of the financial restructuring.

(50) The financial restructuring has been affected by the rescue aid. The outstanding debts at the end of 2020 amounted to HRK 480.8 million (EUR 64.1 million) and included loans from commercial banks, out of which HRK 363.1 million (EUR 48.4 million) were provided under State guarantees. More specifically, at the beginning of 2020, the beneficiary took an additional loan of HRK 150 million (EUR 20 million) from HPB, also under the State guarantee, which has been granted as the rescue aid. The proceeds from this loan were used to refinance the existing loan and to service the due payables to suppliers. In the middle of 2020, the beneficiary used the second part of the rescue aid financed by HBOR, consisting of additional loan of HRK 60 million (EUR 8 million) for operational financing of the freight wagon production. The remaining HRK 153.1 million (EUR 20.4 million) correspond to debt arising from other two loans with a State guarantee as collateral as of 31 December 2020. One is the loan by HBOR for the initial amount of HRK 95 million (EUR 12.7 million), of which HRK 76 million (EUR 10.1 million) are still outstanding, and a loan from HPB amounting HRK 77.1 million (EUR 10.3 million).

(51) The restructuring plan forecasts a twofold reduction of the financial costs, i.e. the beneficiary's debt. First, the conversion of the debt towards the State into equity will entail a reduction of interest expenses. The total amount of debt that will be reduced is HRK […] million (EUR […] million). As a result, the saving per year will be around HRK […] million of interest expenses. Second, the reduction of interest expenses will further decrease the interest on remaining principal. The total residual value of loans principal after the State contribution will be approximately HRK […] million (EUR […] million) saving in reduction of interest rate to 2% amount to approximately HRK […] million (EUR […]) per year.

(52) Additionally, the beneficiary intends to reschedule its remaining debt obligations […].

(53) The expected share capital increase by the new investor will amount to HRK 227 million (EUR 30.3 million). On top of it, the investor has outlined further non-cash contributions to the restructuring process. The assets representing the non-cash contributions are business proven assets, performing well on other markets, and are considered to fit well in the beneficiary's product portfolio, so to add a long-term competitive advantage. They do not require additional material investments to start the production.

Personnel restructuring

(54) The plan assumes an optimisation of the ratio of direct/overhead employees by reducing the organisational complexity and layers of the personnel structure. There are also measures planned to further centralise overhead functions and remove duplications that still exist.

(55) According to the plan, […]. The plan foresees this […] for the reorganisation of production by optimising layout, increasing productivity, and consolidating production programs across the group, which will lead to changes to employee structure […]. Greater synergies within the beneficiary's business activities shall be utilised by establishing centralised business and supporting functions […].

2.4. The State aid measures under assessment

(56) To support the plan, the Croatian authorities have notified restructuring aid in favour of Đuro Đaković for a total amount of HRK 430.6 million (EUR 57.4 million). The restructuring aid will be granted in the form of two aid measures, the first being a debt to equity swap and the other: a State guarantee for potential future claims on the products deficiencies (the "measures"). The content of the measures and a step-by-step implementation mechanism of the debt to equity swap are described below.

a) First State aid measure: Debt to equity swap

The content of the debt to equity swap

(57) The total amount of debt that will be reduced and swapped into equity is HRK […] million (EUR […] million). This debt arises from four outstanding loans:

- the loan in the amount of HRK […] million (EUR […] million) provided by the Croatian Postal Bank (Hrvatska poštanska banka d.d., "HPB") from January 2020;

- the loan in the amount of HRK […] million (EUR […] million) provided by the Croatian Bank for Reconstruction and Development (Hrvatska banka za obnovu i razvoj, "HBOR") from July 2020.

Both of the above loans have been secured by the State guarantee which has been approved as rescue aid (recital (1)). Croatia confirmed that until present, the State guarantee securing rescue aid loans from HPB and HBOR has not been called by the banks, and there is no claim by the State against the beneficiary. The remaining amount of HRK […] million (EUR […] million), which could have covered further loans up to the needs of the beneficiary, was not used as the beneficiary did not take further loans. Therefore, the guarantee initially foreseen to cover up to HRK 300 million (around EUR 40 million) only covered HRK 210 million (EUR 28 million) of loans that the beneficiary took. In addition to the above two loans, the outstanding debt from two earlier loans that the beneficiary took before it entered into difficulty will also be included in the debt to equity swap. This debt concerns the following loans:

- the loan in the amount of HRK […] million (EUR […] million) provided by HBOR in October 2018, of which the outstanding amount is HRK […] million (EUR […] million); and

- the loan in the amount of HRK […] million (EUR […] million) provided by HPB in August 2010.

Both of these loans have been partially secured by the State guarantees granted at the same time.

(58) Given that all these four loans have been fully or partially secured by the State guarantees, and assuming that the guarantees would be called by the banks at a certain point in time, since the beneficiary would not be able to repay the loans, the State decided to support the restructuring of the beneficiary by taking over the outstanding debt arising from these loans. This outstanding debt which will be converted in equity concerns the total amount of HRK […] million (EUR […] million) and stems from the loans under the State guarantee […]. As a consequence, the State will become a debtor *vis-à-vis* banks and creditor *vis-à-vis* the beneficiary. In that way, the State is entitled to a claim towards the beneficiary, on which account it will be able to convert its debt into share capital of the beneficiary.

(59) Once the debts arising from the abovementioned loans are taken over by the State, the State guarantees, including the guarantee that was initially approved as rescue aid and subsequently extended as restructuring aid, pursuant to point 55 d) ii) R&R Guidelines, will come to an end.

(60) Through the debt-to-equity swap and offset of accumulated losses against the share capital, which will be closed with the capital injections by the new investor, the current shareholding structure of the beneficiary will be impacted.

The implementation of the debt to equity swap (including the subsequent share capital increase)

(61) As a first step, the State will acquire existing debts from HBOR and HPB banks, which are secured by the State guarantees. The State will swap the acquired debt into equity of the beneficiary, while the existing shareholders will be diluted as a consequence.

(62) In a second step, the accumulated losses will be offset against the beneficiary's share capital and, consequently, the share capital will be reduced (all shareholders without exception participate in the reduction proportionally to the number of shares held).

(63) Finally, after the share reduction (from 15 203 230 shares to approximately 6 257 666 shares), the new investor DD Acquisition will

increase the share capital with a corresponding increase of shares (to 28 957 666 new shares). DD Acquisition, which is the second largest shareholder, will participate in a share capital increase with a cash and in-kind contributions of HRK 227 million (EUR 30.3 million), as listed in recital (71). At the end of the recapitalisation process, the Croatian State will retain a shareholding of around […] % and will become the second largest shareholder, thus benefitting from the upside of the restructuring and, through its participation in a viable company, ensuring adequate remuneration to its investment through an increase of the value of its holding. Upon the share capital increase, DD Acquisition will acquire up to […] % stake in Đuro Đaković and will become the majority, i.e. controlling, shareholder.

(64) Croatia informs that Đuro Đaković may face claims from the customers on the account of wagon repair due to technical deficiencies. The beneficiary, therefore, needs means to be ready to face such potential claims and possibly litigation costs. The plan foresees that the costs of such potential claims would could go up to HRK […] million (EUR […] million). The State will issue a guarantee to cover a part ([…] %) of the risk of such future potential litigation for an amount up to HRK […] million (around EUR […] million), while the new investor will provide a guarantee to cover such risk up to HRK […] million (EUR […] million). Croatia puts forward that any potential savings or unused amounts out of the guaranteed amount would have a direct impact on the total restructuring costs balance, as well as the share of the State vis-à-vis own contribution portion.

(65) The Croatian authorities informed the Commission that there would be no need for additional restructuring aid.

2.5. Return to viability

Base case scenario

(66) Based upon the base line scenario of the restructuring plan, the beneficiary is expected to return to net profit by the financial year 2022. The total forecasted savings resulting from the operational restructuring are HRK […] million (EUR […] million) with full year effect in 2022, but there are also significant positive impacts expected already in 2021, when major restructuring actions are expected to take place. The expected return on capital employed over the years is presented in the table below (Table 6). Croatia explains that they have used the basic formula in case of return on equity (ROE) and return on capital employed (ROCE) and have also added adjusted ROCE formula. The adjusted ROCE formula is estimated on the basis of the following projection from existing operations and trading: (i) availability of excess cash equal to HRK 15 million (less than EUR 2 million) to reduce debt, and (ii) additional provisions recognized in the balance sheet in 2021 in the amount of HRK 37.5 million (around EUR 5 million) for incurred but reported costs. Both items increase ROCE by reducing the amount of capital employed.

(67) Croatia expects a gradual increase of the sales based on improved efficiency and stabilised liquidity and solvency situation in 2022. The optimisation of the top line assumes that Đuro Đaković will exit the financial difficulties in 2021, allowing it to become a trusted supplier for all its customers. The beneficiary will start implementing a new sales strategy with nine work streams for the sales and engineering departments. These include, among others: (i) selling existing products to new customers, (ii) selling new products to existing customers through better utilization of competencies in technological departments, (iii) selling new products to new customers, leveraging the Đuro Đaković brand (production, competences and machining/assembly capacities) for aftersales parts, and (iv) selling to markets outside the EU.

Table 6: ROCE & ROE, Base case

Base Case

	2021	2022	2023	2024	2025
ROE	[…]%	[…]%	[…]%	[…]%	[…]%
ROCE	[…]%	[…]%	[…]%	[…]%	[…]%
ROCE adj.	[…]%	[…]%	[…]%	[…]%	[…]%

Pessimistic case scenario

(68) In case the pessimistic case scenario occurred, the beneficiary would face negative ROCE in 2021 and 2022, while as of 2023, ROCE would be positive, albeit small, at […] %, while in 2024 it would grow to […] %. The evolution over the years for the pessimistic case is presented in the table below (Table 7).

Table 7: ROCE & ROE, Pessimistic case

	2021	2022	2023	2024	2025
ROE	[…]%	[…]%	[…]%	[…]%	[…]%
ROCE	[…]%	[…]%	[…]%	[…]%	[…]%
ROCE adj.	[…]%	[…]%	[…]%	[…]%	[…]%

(69) In addition to a scenario analysis, Croatia also presented a sensitivity analysis for the restructuring period and beyond to 2025, once the restructuring would be completed. The analysis shows the sensitivity on the key drivers, namely the sales, cost of material and employee costs applied to base case scenarios of ROCE. Given the importance of the return to viability of the beneficiary at completion of the restructuring plan, such estimates are explicitly reported for the year immediately after the restructuring period in the table below (Table 8).

Table 8: Sensitivity analysis

	Low	Base	High
Sales	-5%	0%	5%

ROCE adj 2025	**[…]%**	**[…]%**	**[…]%**

	Low	Base	High
Cost of material	5%	0%	-5%
ROCE adj 2025	**[…]%**	**[…]%**	**[…]%**

	Low	Base	High
Employee costs	5%	0%	-5%
ROCE adj 2025	**[…]%**	**[…]%**	**[…]%**

2.6. Sources of financing of the restructuring plan

(70) The Croatian authorities have identified the sources of financing of the restructuring plan listed in Table 9), totalling HRK […] million (EUR […] million). In particular, the State equity (item (a) in Table 8) covers loans and guarantees received by the beneficiary in 2020 as rescue aid, whereas the guarantee for potential future claims (item (b) in Table 8) is essentially due to the insufficient quality of delivered products in the past years, which the investor has agreed to pay in part (item 5 in Table 8). DD Acquisition, as the second biggest shareholder, will participate in a share capital increase with a cash and in-kind contributions of total HRK 227 million (around EUR 30.3 million). The overall own contribution from the beneficiary and the new investor amounts to HRK […] million (around EUR […] million) and supports 52.74% of the restructuring costs.

(71) As summarised in Table 9, the own contribution by the investor consists of both a capital increase and a non-financial contribution with immediate impact on productivity (item 3 in Table 9), as well as facilitation for new contracts (item 6 in Table 9). The investor will also replace the State, upon expiry of HBOR guarantee scheme (recital 135), in a new guarantee scheme of HRK […] million for the commercial guarantees to the company’s customers (item 2 in Table 9) and will bear the consulting fees for the restructuring process (item 4 in Table 9), as well as the costs that might arise from contractual and litigation claims (including penalties for delayed wagons and expenditure for serial wagon modifications) concerning faulty products previously manufactured by the beneficiary (item 5 in Table 9). In addition, the investor will secure financing on commercial basis for further capital expenditure to fund investment in machinery and equipment, in particular, in the transport segment (item 8 in Table 9). The beneficiary, on its part, will contribute with the sale of various non-core assets (including plots of land and apartments) and severance payments following labour reorganization (respectively, items 1 and 7 in Table 9).

Table 9: Sources of financing of the restructuring plan in HRK million

State aid	
a. State claim converted to equity	[…]
b. State guarantee for potential future claims	[…]
Own contribution	
1. Sale of the non-core assets	[…]
2. Financial guarantee	[…]
3. Investor's share capital contribution to working capital, material and non-material assets	[…]
4. Consulting fees and costs pertaining to restructuring plan/process	[…]
5. Future potential contractual / litigation claims (max cap)	[…]
6. Future contracts - financial guarantee of new contracts performance, secured by the Investor	[…]
7. Severance payments contribution	[…]
8. Further investment (CAPEX) by Investor	[…]
Total own contribution (52.74%)	**[…]**
Total State aid and own contribution	**[…]**

Source: Đuro Đaković's Restructuring plan of 23 November 2021

2.7. Measures to limit distortion of competition

(72) First, as a structural measure, the beneficiary will withdraw from the market for industrial solutions and liquidate the subsidiary Đuro Đaković Industrial Solutions, active thereon with a track record of profit, either as sole service provider or often in different consortia. As a major contributor and key driver to the beneficiary's revenues, Industrial solutions generated 26% of the total consolidated revenues of Đuro Đaković Group in 2019. By exiting the market, Đuro Đaković will allow domestic and foreign competitors - especially those present at regional and national level, such as Monting Ltd., ĐĐ Montaža Ltd., Zagreb-montaža Ltd., ĐĐ TEP Ltd., M-SAN Ltd. or Končar KET Ltd. - to fill the gap.

(73) As a second measure, the beneficiary commits not to extend its overall production capacity over the current constraint and keep it below full

utilisation, at the level of 1.000 wagons a year for the duration of the restructuring plan. Croatia explains that the annual production capacity constraint of 1 200 – 1 400 wagons annually is defined by the limiting capacity of the paint shop, the main bottleneck of the production. This is to say that this overall yearly production capacity depends on the level of sophistication of produced wagons. Currently, there are production cycle constraints that prevent technological production capacity from being fully utilised. This is attributable primarily to a blasting box. The restructuring plan foresees an investment into the blasting box which will improve work efficiency (and profitability), in addition to new contracted sales, reorganisation of the shop floor cycle, as well as its optimised layout. Croatia puts forward that, since the market is growing in terms of freight, specifically new technologies are being developed with significant demand for intermodal wagons, as well as promoting support of Green deal to rail freight transport, the beneficiary may achieve a growth in meeting such demands. Notwithstanding this potential for further growth, the beneficiary is willing to limit its overall production capacity output to 1 000 wagons a year.

(74) As a third measure, the beneficiary commits to discontinue production, marketing and sales during the restructuring period, as well as beyond, of three types of wagons. Out of these, two are tank wagons, type "Zacns 45" for transportation of CaCO3 slurry and type "Uacns 74" for transportation of dry bulk cement. As a third wagon, the beneficiary will discontinue the production of the open wagons, type "Eanos (s)", which is designed for transportation of coal, coal coke, iron ore, sand and similar goods. Croatia explains that these wagons are mainly operated in Poland and Eastern Europe for transport of coal and of similar products.

(75) Altogether, these wagons have an annual potential production of 300 pieces and represent the beneficiary's turnover of EUR […] million. Croatia informs that the beneficiary will deliver the remaining wagons which it has already contracted.

(76) Croatia puts forward that there is a very limited number of manufacturers that produce these wagon types, which are in demand. According to Croatia, by discontinuing production of these types of wagons, the beneficiary leaves a major spot on the niche market for other competitors to fill. In the absence of precise data for each wagon type, Croatia has provided data for the overall European freight wagons procurements in the Restructuring Plan of 23 November 2021[17]. According to the data submitted by the Croatian authorities, the European freight wagons procurements would amount to around 12 000 units in 2021-2024, so that the aggregated reduction (200+300 units) offered by the beneficiary would be around 4% of the new wagon production in the EU, where the beneficiary would have a market share

[17] SCI Forecast data.

of around 8% (1 000 units/year) and, due to the cap undertaken as structural measure, such presence would not be reinforced by the aid in the restructuring period.

(77) Finally, Croatia provides a commitment that Đuro Đaković will refrain from acquiring shares in any company, during the restructuring period, except where it is indispensable to its long- term viability in which case it will notify the Commission and will not publicise the restructuring aid as a competitive advantage.

3. ASSESSMENT OF THE MEASURES

3.1. Existence of State aid

(78) According to Article 107(1) TFEU, "*save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects the trade between Member States, be incompatible with the internal market*".

(79) It follows that, for a measure to be qualified as State aid within the meaning of Article 107(1) TFEU, the following cumulative criteria must be met: (i) it must be granted by the State and through State resources; (ii) it must confer an advantage upon an undertaking; (iii) it must be selective, i.e. favour certain undertakings or the production of certain goods; and (iv) it must distort or threaten to distort competition and it must affect trade between Member States.

3.1.1. State resources and imputability to the State

(80) The measures in question, the planned capital contribution, i.e. the HRK […] million (EUR […] million) in the form of debt to equity swap referred to in recital (56), will be implemented following a decision by the Croatian Government, while the State guarantees, which secured the debt to be converted in equity, have stemmed as an obligation to the central State budget and, consequently, the taking over of this debt before its conversion into equity also burdens the central State budget. The proposal for the issuance of HRK […] million (EUR […] million) State guarantee to cover possible future litigation costs (recital (64)) has been made by the Ministry of Economy and Sustainable Development, while the guarantee will be issued by the Government and implemented by the relevant Ministry. The funds will be available through the budget of the State. Therefore, the debt to equity swap and the State guarantee in total of HRK […] million (EUR […] million) are imputable to the State and involve State resources.

3.1.2. Advantage

(81) An advantage, within the meaning of Article 107(1) TFEU, is any economic benefit, which an undertaking would not have obtained under

normal market conditions, that is to say in the absence of State intervention[18].

(82) As referred in recitals (57) and (64), the debt to equity swap and the State guarantee confer an economic advantage to Đuro Đaković allowing it to continue its operations without bearing all of its financial costs and to escape insolvency by providing funding that Đuro Đaković, given its critical financial state, has not been able to obtain on the market. Croatia has not claimed that the abovementioned decisions were taken on the basis of economic evaluations comparable to those which, in similar circumstances, a rational market economy operator with characteristics similar to those of the Croatian Government would have had carried out to determine the profitability or economic advantages of the measures, before deciding on the purported investment ("market economy operator test"). Even if such a test were applicable, *quod non*, the assessment of whether a market operator in a situation as close as possible to that of Croatia would provide the same funding shows that the public funding in question provides an advantage with regard to market conditions. First, the public funding is premised on reasons of public policy to guarantee the employment level in a structurally weak economic area (NUTS 2 region of Panonska Hrvatska) (recitals (23)-(24)) and the development of activities with higher technological input. Secondly, except DD Acquisition, which will hold a controlling stake in the beneficiary, no other shareholder than the State contributes to the cost of restructuring, thus indicating that the expected returns are insufficient. Thirdly, given the present losses, the cumulated return on the equity contributed by the Croatian State between 2020, when the rescue aid was granted, and 2023 - and beyond until 2024 - is below the reference which the Commission deems adequate to conclude on the long-term viability of the beneficiary (recitals (33-35) and recital (36)).

(83) It follows that the measures at issue confer an advantage to Đuro Đaković within the meaning of Article 107(1) TFEU.

3.1.3. Selectivity

(84) Article 107(1) TFEU also requires that a measure, in order to constitute State aid, is selective in the sense that it favours "*certain undertakings or the production of certain goods*".

(85) In this case, the measures at issue are granted through the exercise of discretion to the benefit of one specific undertaking, Đuro Đaković, to assist and support its restructuring, and are not part of a broader measure of general policy and application that would be available to all undertakings in Croatia. As the Court stated, where individual aid is at issue, the identification of the economic advantage is, in principle, sufficient to support the presumption that a measure is selective.[19]

[18] Judgment of 11 July 1996, *SFEI and others*, C-39/94, EU:C:1996:285, paragraph 60; judgment of 29 April 1999, *Spain v Commission*, C-342/96, EU:C:1999:210, paragraph 41.

[19] See judgment of 4 June 2015 *Commission* v *MOL*, C-15/14 P EU:C:2015:362, paragraph 60.

Moreover, in light of the objective pursued, the capital contribution as a result of a debt to equity swap and the State guarantee are granted on an entirely *ad hoc* basis to a single beneficiary and similar funds are not available to other undertakings, in a comparable legal and economic situation, active in the wagon production or in other sectors. This is so regardless of whether there are operators on the relevant markets that are in a comparable factual and legal situation. The debt to equity swap and the State guarantee are therefore selective measures.

3.1.4. Distortion of competition and effect on trade

(86) If the aid granted by a Member State strengthens the position of an undertaking compared to other undertakings competing in intra-Union trade, the latter must be regarded as affected by that aid.[20]

(87) As explained in recital (16), the restructuring aid granted to Đuro Đaković affects the production of the rail freight wagons and spare parts production activities. The industrial activities relating to production of rail freight wagons, in which Đuro Đaković is active, are open to competition and trade between Member States and there are several other undertakings active in this business activity throughout the Union, as referred to in recital (17).

(88) Therefore, the advantage granted to Đuro Đaković is likely to distort competition and affect trade between Member States.

3.1.5. Conclusion on the existence of State aid

(89) For the reasons set out above, the Commission concludes that the measures involve State aid within the meaning of Article 107(1) TFEU and will therefore assess lawfulness and compatibility of those measures with the internal market.

3.2. Lawfulness of the measures

(90) Croatia has prolonged the State guarantee for as long as the loans secured by such guarantee have not been paid back. The restructuring plan assumes a conversion of such State-guaranteed loans into equity. Therefore, the State guarantee, first granted as unlawful rescue aid (recitals 26-27 of the rescue aid decision), becomes part of the restructuring aid for the amount of HRK […] million (EUR […] million) by which it has covered two loans, one for HRK […] million (EUR […] million) in January 2020, and the other for HRK […] million (EUR […] million) in July 2020, as the State-guaranteed loans will be converted into equity (recital (56-57)). Croatia communicated to the Commission the restructuring plan of Đuro Đaković on 30 June

[20] See, in particular, judgment of 17 September 1980, *Philip Morris v Commission*, 730/79, EU:C:1980:209, paragraph 11; judgment of 22 November 2001, *Ferring* C-53/00, EU:C:2001:627, paragraph 21; judgment of 29 April 2004, *Italy v Commission* C-372/97, EU:C:2004:234, paragraph 44.

2021, meaning more than a year after the granting of the rescue aid (recitals (2) and (4)). Point 55(d) of the R&R Guidelines, interpreted in light of Article 108 (3) TFEU, requires that the restructuring plan be notified to the Commission in a version, which would allow a complete assessment of its compliance with the R&R Guidelines, before the restructuring aid has been put in effect. The restructuring plan, as initially submitted on 30 July 2020, did not entail key elements of the plan sufficiently defined to take position on compliance of the plan with the R&R Guidelines, such as the identity and amount of effective (equity) contribution of the possible strategic investor(s), their adherence to the plan and restructuring actions envisaged therein, the situation and absorption of losses by current shareholders etc. Therefore, the submission of that draft restructuring plan entailing restructuring aid did not formally meet the required legal standard to qualify as notification under the Procedural Regulation.

(91) Accordingly, Croatia did not observe the stand-still obligation laid down in Article 108(3) TFEU and the restructuring aid to the benefit of Đuro Đaković constitutes unlawful State aid since July 2020.

3.3. Compatibility of the aid

(92) Article 107(3)(c) TFEU provides that State aid can be authorised where it is granted to promote the development of certain economic sectors or certain economic areas and where such aid does not adversely affect trading conditions to an extent contrary to the common interest.

(93) Croatia submits that the restructuring aid would be compatible with the internal market on the basis of Article 107(3)(c) TFEU, and in particular as restructuring aid under the R&R Guidelines.

(94) The assessment of the compatibility with the internal market must therefore involve the examination whether the conditions of the R&R Guidelines for granting restructuring aid are met. Moreover, it does not result from the notification that the restructuring aid to Đuro Đaković, the conditions attached to it, or the economic activities facilitated by the aid, could entail a violation of any Union law provision. In particular, the Commission has not sent a reasoned opinion to Croatia on a possible infringement of Union law that would bear a relation to this case and the Commission has not received any complaints or information that might suggest that the State aid, the conditions attached to it or the economic activities facilitated by the aid might be contrary to any Union law provisions.

3.3.1. Eligibility

Undertaking in difficulty

(95) In order to be eligible for restructuring aid, an undertaking must qualify as an undertaking in difficulty pursuant to section 2.2 of the R&R Guidelines. In particular, point 20 of the R&R Guidelines stipulates that an undertaking is considered to be in difficulty when, without intervention by the State, it will almost certainly be condemned to

going out of business in the short or medium term. This would be the case when at least one of the circumstances described in point 20 from letter a) to d) of the R&R Guidelines occurs.

(96) As explained in recital (33), more than half of Đuro Đaković`s subscribed share capital has disappeared as a result of accumulated losses and the beneficiary had a negative equity at the end of 2019, when the Commission assessed the State guarantee in the rescue aid decision. The beneficiary still posted negative equity in 2021, according to the financial reports for the first quarter, and accumulated further losses in the first 8 months of 2021 (recital (35)). Moreover, also the ratios assessed under point 20 d. of the R&R Guidelines show Đuro Đaković has been undertaking in difficulty since the granting the rescue aid. The beneficiary's debt to equity ratio was -2.47 on 31 December 2020 and EBITDA interest coverage ratio was -1.07 on 31 December 2020. Đuro Đaković, thus, qualifies as an undertaking in difficulty pursuant to point 20(a) of the R&R Guidelines since July 2019.

(97) According to point 21 of the R&R Guidelines, a newly created undertaking is not eligible for restructuring aid. An undertaking is in principle considered as newly created for the first three years following the start of operations in the relevant field of activity. Đuro Đaković is not a newly created undertaking since it was established in 1991 (see recital (7)).

(98) Point 22 of the R&R Guidelines provides that a beneficiary belonging to or being taken over by a larger business group is not normally eligible for rescue or restructuring aid, except where it can be demonstrated that the company's difficulties are intrinsic and are not the result of an arbitrary allocation of costs within the group. As explained in recital (7) of the present decision and recital 32 of the rescue aid decision, Đuro Đaković is a group on its own and is not part of a larger business group. The State was the main shareholder and adopted the beneficiary's strategic decisions for most of the existence of the company, although its presence in the capital shares was progressively diluted and went from 50.66% of the capital shares in 2016 to 37.86% in 2018 and to 26.4% currently. By 2019, when the beneficiary's difficulties arose, therefore, the State was no longer the majority shareholder, but was only one of the largest stakeholders along with two individuals (recital (8)). In November 2020, following the acquisition of a minority shareholding (18.9%) by DD Acquisition the shareholding structure of the beneficiary changed in comparison to the point in time when rescue aid was approved, as described in Table 1. However, that acquisition and change at the level of a second largest shareholder by transfer of 18.9% shares from physical persons to the DD Acquisition does not imply that Đuro Đaković has entered into a larger business group (because it was still not under the sole or joint control of any other entity, see recital (9)), nor that the new private investor could arbitrarily pass-on costs to Đuro Đaković. This even more so as the beneficiary's economic and financial difficulties derive from past business strategies that largely predate DD Acquisition's

entry into the corporate structure. As the new private investor will become the controlling shareholder (with around 80% of the share capital) only after the completion of the share capital increase, it can be concluded that neither at present, nor at the time when the difficulty arose, Đuro Đaković has been part of a larger business group and its difficulties have not been a result of an arbitrary allocation of costs within a group. Moreover, there was no larger business group to which the beneficiary has belonged and which should have potentially have dealt with the difficulties of the beneficiary.

(99) On the basis of the above, the Commission concludes that Đuro Đaković is an undertaking in difficulty which has not been part of a larger business group and is eligible for restructuring aid.

3.3.2. *Contribution to the development of an economic activity or an economic area*

(100) State aid granted under Article 107(3)(c) TFEU must be intended to facilitate the development of certain economic activities or certain economic areas[21]. In the specific context of rescue and restructuring aid, the Commission notes that, as acknowledged at point 43 of the R&R Guidelines, in fact, market exit is important to the wider process of productivity growth, thus merely preventing an undertaking from exiting the market does not sufficiently justify State aid. On the contrary, rescue and restructuring aid are among the most distortive types of State aid, as they interfere with the process of market exit.[22] However, in certain situations, restructuring an undertaking in difficulty may contribute to the development of economic activities or areas, also beyond the very activities carried out by the beneficiary. This is the case where in the absence of such aid, the beneficiary's failure would lead to situations of market failure or social hardship, inhibiting the development of the economic activities and/or areas that would be affected by such situations. A non-exhaustive[23] list of such situations is laid down at point 44 of the R&R Guidelines. By enabling the beneficiary to continue its operations, the aid prevents such market failure or social hardship. In case of restructuring aid, this is however only true where the aid indeed enables the beneficiary to compete in the marketplace on its own merits, which can only be ensured if the aid is accompanied by a restructuring restoring the beneficiary's long-term viability.

(101) The Commission will thus first assess whether the aid is intended to prevent a situation of market failure or social hardship (section 3.3.2.1)

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21 See judgment of 22 September 2020, C-594/18 P, *Austria v Commission*, , EU:C:2020:742, paragraphs 20 and 24.

22 Point 6 of the R&R Guidelines.

23 The list begins with an "*in particular*" and ends with a reference to "*similar situations of severe hardship duly substantiated by the Member State*" at point 44(g) of the R&R Guidelines.

and whether it is accompanied by a restructuring plan restoring the beneficiary's long-term viability (section 3.3.2.2).

3.3.2.1. Prevention of market failure or social hardship

(102) Among the situations where rescuing an undertaking in difficulty may contribute to the development of economic activities or areas, point 44(a) and (c) of the R&R Guidelines mention cases where aid is intended to avert the risk of economic growth being hampered by the failure of an undertaking that either is located in a region where unemployment is higher than Union or national averages, persistent and accompanied by difficulty in creating new jobs (point 44(a) of the R&R Guidelines), or has an important systemic role in a particular region or sector (point 44(c) of the R&R Guidelines).

(103) As described in recital (7), Đuro Đaković is a metal mechanical engineering group based in Croatia, which manufactures products both for civil and military use, in the area NUTS 2 Panonska Hrvatska (HR02) that has consistently had a higher unemployment rate compared to the EU-27 average, accompanied by structural problems of job losses and new jobs creation (recital (23)). In fact, the unemployment data concerning that region, as measured in Eurostat data until the end of 2020 (Table 4), does not fully reflect the seriousness of the region's situation, given that it was measured for the entire continental Croatia (the region previously identified as HR04), which is a very diversified area, with the western part, together with the capital Zagreb, being more advanced while the Eastern part, including Brod-Posavina County, in which Đuro Đaković has its headquarters, being far less developed (recital (24)). In fact, the Brod-Posavina County (NUTS 3 code HR24) is the county with the highest unemployment rate in entire Croatia, nearly the double of the country's unemployment rate and more than double of the EU-27 average in 2020.

(104) The presence of Đuro Đaković in this structurally weak region has been of utmost importance, first, directly as a provider of jobs to more than 700 people, currently with plans to increase the said number of jobs, and second, indirectly as a provider of jobs to other companies, such as its suppliers, which are mainly located in the area. The market exit of Đuro Đaković as one of very few technology companies in the affected area would leave such knowledge and expertise unused and the long on-going cooperation and dependency of the education system and systemic approach to developing skilled human capacities that have a logical sequence from education system to employment with Đuro Đaković would be disrupted (recital (24)).

(105) Moreover, based on the information provided by Croatia on the sector and the referred structural weaknesses of the region in which Đuro Đaković is located (Panonska Hrvatska)[24], it is likely that the

[24] https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Labour_market_statistics_at_regional_level#Unemployment.

bankruptcy of Đuro Đaković would trigger severe social hardship in the short term on the labour force, suppliers and customer chain, as well as on families dependent upon its undisrupted operations. As is referred to in recital (25), the production facility and employees are of great importance for the local job market and small and medium suppliers which depend on Đuro Đaković. For these reasons, it can be concluded that Đuro Đaković is deeply integrated in the local economy needs and that its failure would be likely to involve serious social and economic hardship within the meaning of point 44(a) of the R&R Guidelines.

(106) Finally, given the particular nature and characteristics of the production related to the military sector, the failure of Đuro Đaković would leave a most sensitive area of the public administration without its current provider of spare parts and services (in particular, for the Patria and Kongsberg vehicles still in use in the State defence). Such activity could not be diverted to competitors, which are neither present in the affected region nor in Croatia (recitals (22) and (25)). In the light of the importance and specificity of the input provided by the beneficiary to the Ministry of Defence, as well as the fact the Đuro Đaković is the sole domestic undertaking providing such goods and services in the sector, hence, the aid prevents the market exit of a supplier of an important input within the meaning of point 44(c) of the R & R Guidelines.

(107) The Commission notes that the State may support the military production for the purposes of the national security according to Article 346(1)(b) TFEU. Croatia has provided a commitment for the military and civil productions of the beneficiary to be fully separated after the end of the restructuring period (recital (22)). Since other markets on which the beneficiary is active, in particular the rail freight market, are open to competition, the cross-subsidisation has to be excluded, which requires that separate accounts are used, costs and revenues are allocated in an appropriate way and public funding provided for the military production must not benefit other activities.

(108) In the view of the above, the Commission considers that the notified restructuring aid supports the development of certain economic activities and areas, as required by Article 107(3)(c) TFEU. Namely, the aid seeks to prevent the failure of an undertaking which is deeply integrated in the economy of the NUTS 2 region of Panonska Hrvatska (HR02), and in particular of the Brod-Posavina county (HR24), and which serves an important systemic role in the provision of parts for certain military vehicles and in servicing those vehicles, as the only Croatian undertaking providing such goods and services.

3.3.2.2. Restoration of long-term viability

(109) According to point 45 of the R&R Guidelines, a Member State wishing to grant restructuring aid must submit a restructuring plan aimed at

restoring the beneficiary's long-term viability. According to point 46 of the R&R Guidelines, the granting of the aid must be conditional on implementation of the restructuring plan which the Commission must endorse in all cases of *ad hoc* aid. According to point 47 of the R&R Guidelines, the restructuring period must be as short as possible and the restructuring plan must restore the long-term viability of the beneficiary within a reasonable timescale based on realistic assumptions.

(110) According to point 48 of the R&R Guidelines, the plan must identify the causes of the beneficiary's difficulties and outline how the proposed restructuring measures will remedy the beneficiary's underlying problems. Long-term viability is achieved when the beneficiary is able to provide an appropriate projected return on capital after having covered all its costs including depreciation and financial charges (point 52 of the R&R Guidelines).

(111) Đuro Đaković's restructuring plan, described in section 2.3, has been designed to tackle the difficulties identified by the beneficiary after a thorough assessment of the reasons for its financial difficulties (see recitals (39) to (31)) and with the purpose to make it viable again.

(112) The plan refocuses and downsizes the activities, whilst ensuring that Đuro Đaković will return to long-term viability and provide an appropriate return on capital around […] % by generating a positive cash flow from the year 2022, under the base scenario, and from the year 2024, under the pessimistic case scenario (recitals (68) and Table (7)). Therefore, it can be realistically expected that the beneficiary will not need more State aid after the restructuring.

(113) The 4-year duration between 2020 and 2024 is not unreasonably long, given that the beneficiary has been overburdened with debt and the financial results of the company need this period to stabilise. In that regard, the restructuring plan thoroughly identifies the reasons for the troubles of Đuro Đaković. As a consequence, the new investor will immediately start with the operational restructuring by contributing not only the cash, but also non-cash capital contributions (recital (53) and Table 9), which with synergies, experience, and market knowledge of the new majority shareholder are able to improve the profitability and sustainability of the beneficiary.

(114) Moreover, the Commission has carefully reviewed the key assumptions underlying the financial forecasts of the restructuring plan submitted by Croatia. In particular:

a) The beneficiary is expected to return to net profit in financial year 2022. The total forecasted savings resulting from the operational restructuring are HRK […] million (EUR […] million) with full year effect in 2022, but there are also significant positive impacts expected as from 2021, when major restructuring actions, such as the implementation of the sales strategy, which includes work streams for the sales and engineering organisation, as well as the financial restructuring related to the loans repayments with plans for HRK […]

million (EUR […] million) to be repaid by the end of 2021, have already taken place.

b) The cause of the liquidity problems of Đuro Đaković was predominantly of a technical and operational nature, due to the lack of the technical know-how to manufacture the wagons, which resulted in delays, cost overruns and penalties for late deliveries, which has its roots in earlier strong dependence on military segment. With the new investor, the beneficiary will continue a much-needed substantive transformation and will undertake investments such as blasting box (recital (73)).

c) The forecasts of operating costs for the period 2020-2023 adequately take into account the increased operating costs in accordance with the new production plan prepared by the new investor, which aims at supporting the sales process to make profitable sales and avoid situation of either losing opportunities due to higher than competition prices or making an unprofitable sale as it was the case in the past (see recital (44)).

d) Other costs, notably financial expenses related to interest and principal payments, are in line with the planned financial restructuring measures (see recital (49-53)).

e) The restructuring plan forecasts a gradual increase of the sales based on improved efficiency and stabilized liquidity and solvency situation in 2022. The optimisation of the top line assumes that Đuro Đaković will exit the financial difficulties in 2021 allowing it to become a reliable supplier.

(115) In accordance with point 50 of the R&R Guidelines, the Croatian authorities have prepared a pessimistic scenario (see recital (68)) on the potential development of Đuro Đaković's operations. It takes into account the reduction in sales of -5.0% per year from 2021 to 2025 compared to the base scenario. In 2021 this includes cutting- off of the already made orders of certain customer programmes, as situation with COVID-19 pandemic situation evolves. The pessimistic scenario also assumes that the prolonged State aid and the ongoing acquisition process might have an adverse effect on sales as customers might lose confidence in Đuro Đaković delivering on time.

(116) In view of the above, the Commission concludes that the proposed restructuring plan is feasible, coherent and far-reaching, and is capable of restoring the long-term viability of Đuro Đaković within the proposed restructuring period, the length of which is reasonable.

3.3.3. *The aid measure must not unduly affect trading conditions to an extent contrary to the common interest*

(117) In examining whether a State aid measure has an adverse effect on trading conditions to an extent that is contrary to the common interest, the Commission carries out a balancing test according to Article 107(3)(c) TFEU and the R&R Guidelines. In that test, the Commission

weighs the positive effects of the aid for the development of the activities and/or areas that that aid is intended to support (as identified in section 3.3.2) against the negative effects created by the impact of the State aid on competition and trade between Member States. In assessing such negative effects, the Commission must satisfy itself that the distortive impact of the aid on competition is sufficiently limited, though the criteria of necessity, incentive effect, appropriateness, proportionality, transparency, the compliance with the 'one time, last time' principle and through the presence of measures further limiting the distortions of competition generated by the aid.

3.3.3.1. Need for State intervention, incentive effect and appropriateness

Need for State intervention and incentive effect

(118) Under point 53 of the R&R Guidelines, Member States that intend to grant restructuring aid must provide a comparison with a credible alternative scenario not involving State aid, demonstrating how the objective sought by the aid would not be attained or would be attained in a lesser degree, in case of that alternative scenario.

(119) Croatia maintains that the rescue aid has had a clear incentive effect in that the shareholders at that time would not have been able to avert the insolvency. Đuro Đaković faced urgent liquidity needs at the end of 2019 and beginning of 2020. The rescue aid provided the possibility for the beneficiary to access the funds for urgent liquidity. These funds were used to cover the cash gap due to lack of support from banks. As already stated in the rescue aid decision (recital (29)), without the rescue aid, the beneficiary would not have survived beyond one month.

(120) The restructuring plan for Đuro Đaković states that there are no feasible alternative scenarios that could restore its long-term economic viability. More specifically, it would not be feasible for Đuro Đaković to restore viability by changing the focus from the rail freight wagon production as this is the segment in which the beneficiary found a niche with good prospects for achieving profitability.

(121) As referred to in recital (39), Đuro Đaković has started a restructuring process that is planned to end in 2024, in order to restore its long-term profitability. To support the plan, the Croatian authorities have notified restructuring aid in favour of Đuro Đaković consisting of the debt to equity swap equal to HRK […] million (EUR […] million), which also included originally granted State guarantee as rescue aid, as well as a State guarantee of up to HRK […] million (EUR […] million) to cover the costs in cases of possible future litigation due to technical deficiencies. In order to ensure long-term viability of Đuro Đaković, the new investor will in particular undertake operational restructuring that will address all weaknesses in the current operations and optimise the production allowing the beneficiary to become profitable (recital (47)).

(122) Based on the information provided, the Commission concludes that the measures are necessary to avert a failure of the beneficiary, and by doing so, to facilitate the development of the economic activities and areas which the aid seeks to support.

Appropriateness

(123) According to point 54 of the R&R Guidelines the Commission will not consider an aid measure to be compatible with the internal market if other, less distortive measures allow the same objective to be achieved. In this respect, restructuring aid must fulfil the conditions laid down in point 58 of the R&R Guidelines. The instrument chosen must be appropriate to the issue that it is intended to address.

(124) Given the beneficiary's accumulated losses, its weak solvency position and the need for liquidity, the State performing the debt to equity swap will enhance the equity and addresses these weaknesses. This State aid measure is a logical consequence of the State having been a shareholder while the beneficiary accumulated these losses, meaning the State acting responsibly along with the new investor entering into share deal and taking over the responsibilities of a shareholder. On that account, the debt to equity swap properly addressing the beneficiary's problems is appropriate as required by point 58 of the R&R Guidelines. As regards the guarantee for the future litigation risk, it is appropriate because the State will only face an expenditure where such risks emerge, so no immediate payment is involved upfront, and the investor also shares part of this risk. This makes also this aid measure an appropriate aid instrument within the meaning of point 58 of the R&R Guidelines. Croatia also confirmed that Đuro Đaković will not need additional financing (see above recital (65)).

(125) The Commission therefore concludes that the measures are appropriate.

3.3.3.2. Proportionality of the aid, own contribution and burden sharing

(126) Under point 61 of the R&R Guidelines, the amount and intensity of restructuring aid must be limited to the strict minimum necessary to enable restructuring to be undertaken, in the light of the existing financial resources of the beneficiary, its shareholders or the business group to which it belongs. In particular, a sufficient level of own contribution to the costs of the restructuring and, where State support is given in a form that enhances the beneficiary's equity position, burden sharing must be ensured. Assessment of those requirements will take account of any rescue aid granted beforehand.

(127) The own contribution must be real and actual and should normally be comparable to the aid granted in terms of effect on the solvency or liquidity position of the beneficiary. Pursuant to point 63 of the R&R Guidelines, the Commission needs to assess whether the various sources of own contribution to the restructuring plan are aid-free, in particular those provided by the State. According to point 64 of the

R&R Guidelines, the own contribution can be considered to be adequate if it amounts to more than 50% of the restructuring costs.

(128) The non-repaid rescue aid was used to meet urgent operating costs during the rescue phase (recital (30)). Not reimbursing this loan has alleviated Đuro Đaković's liquidity needs. Except for that, the majority of the restructuring costs are covered with own resources (recitals (70) and (71)).

(129) The level of own contribution of 52.74% (around EUR […] million) to the costs of implementation of the restructuring plan (around EUR […] million) is higher than the 50% minimum required and is composed of the elements described below.

(130) On the one hand, the new investor commits to inject HRK […] million (EUR […] million) to the beneficiary's share capital by both monetary and non-monetary contributions (item 3 in Table 9). Within that amount, the investor will make a cash contribution of HRK […] million (EUR […] million). As non-monetary contribution, the investor will transfer a total value of HRK […] million (EUR […] million) of tangible and intangible assets in form of intellectual property, technical documentation, production applications etc. Those assets are estimated on the basis of the financial accounts of the investor and, further to the completion of the transaction, are subject to independent appraisal for review and validation by the commercial court. On that basis, these contributions are real, that is to say actual which qualifies them for own contribution within the meaning of the point 63 of the R&R Guidelines. In addition, a portion of available cash from the investor's contribution will be needed to settle the estimated HRK […] million (EUR […] million) of due interest and fees related to the funding provided within the rescue aid.

(131) On the other hand, the beneficiary itself will pay from its own sources stemming from the current revenues and in that way the beneficiary contributes with these severance payments to the restructuring costs (item 7 in Table 9). The restructuring plan has estimated the severance costs of up to HRK […] million (EUR […]). These costs are pertinent to the personnel restructuring foreseen by the restructuring plan and are immediate, as the personnel reorganisation has been inseparable to the optimisation of the production (recital (44)). The costs for severance payments will be paid by the beneficiary from its own funds earmarked for this restructuring expense in the beneficiary's revenues.[25] In other words, these costs will not be financed by State aid, neither from the equity nor from the State guarantee for future litigation costs. Therefore, the beneficiary's contribution to these costs can be regarded as its own, while being real, that is to say actual within the meaning of point 63 of the R&R Guidelines.

[25] In 2020, the total consolidated revenues of the beneficiary amounted to HRK 393.5 million, which is HRK 112.6 million, or 40.08 percent more than in 2019, while total expenses grew much slower, by 1.75 percent, to HRK 454.7 million.

(132) Furthermore, both the investor, as well as the beneficiary, will pay for professional fees and other costs necessary to support management and in the ongoing restructuring planning and execution (item 4 in Table 9). These costs amount to total approximately HRK […] million (EUR […]).

(133) In addition, the new investor commits to secure financing for additional capital expenditures ("CAPEX", item 8 in Table 9)[26], on top of the cash and non-cash contributions invested in equity, totalling HRK […] million (EUR […] million), for investment in machinery, mainly in the transport segment, which are needed to meet the business plan requiring the beneficiary's return to viability. These investments are worth HRK […] million (EUR […] million). Given the firm commitment supported by a description of the underlying expenditures in the restructuring period, this additional capital expenditure can be accepted as actual own contribution by the investor.

(134) As for the future contracts to be brought by the investor (item 6 in Table 9), the investor firmly committed to sign an agreement with one of the subsidiaries for a production and delivery to a known customer of 100 intermodal (container) wagons, which will be produced and delivered during the restructuring period. The estimated amount of HRK […] million (EUR […] million) represents an amount of financing, which the investor committed to secure from an independent financial institution related to this particular agreement. Hence, as these contracts are financially secure, and their relative amount represents activities reserved for the beneficiary during the restructuring period, they can be considered real and actual, the Commission can account them for own contribution.

(135) In respect of the proceeds of the sale of non-core assets (item 1 in Table 9), as they appear to be a conservative estimate based on current market value and relate to solid assets (mainly real estate), for which possible buyers are likely to be found in a reasonable timeframe, the Commission considers that they can be considered as a valid, real and actual contribution by the beneficiary. The same conclusion can be reached for the financial guarantee for which the investor has firmly committed to replace the HBOR's guarantee of HRK […] million for the operational financing of freight wagon production once that guarantee expires (item 2 in Table 9), given that it appears an aid-free support, as well as the investor's commitment to bear part of the costs relating to possible future litigation and contractual claims for faulty production (item 5 in Table 8), where such costs are proportionally shared with the State.

[26] CAPEX or capital expenditures are funds used by a company to acquire, upgrade, and maintain physical assets such as property, plants, buildings, technology, or equipment. CAPEX is often used to undertake new projects or investments by a company.

(136) On that basis, the Commission concludes that the restructuring aid is proportionate with the own contribution above 50% of the restructuring costs (recital (129)).

(137) The State will swap the debt into equity, while other shareholders will be diluted, so that the accumulated losses will be off-set and, consequently, the share capital will be reduced. All shareholders participate in the offset proportionally to the number of shares held (Table 5). As the shareholders, who currently hold 54.7% of the beneficiary's share capital (i.e. all shareholders apart from the State and the investor) (Table 1), will eventually be reduced to a 0.22% shareholding (Table 5), the burden sharing is adequate pursuant to point 66 of the R&R Guidelines.

(138) Finally, after the recapitalisation by the investor (Table 5) the State will still hold a stake in the beneficiary (of around 20%). Even though this represents a minority shareholding, the State is able, upon the finalisation of the restructuring process, to exploit the benefits of dividend yields and growth of the beneficiary's value. This will afford the State a reasonable share of future gains in value of the beneficiary which will become viable, i.e. a profitable, company, as a result of restructuring. Therefore, the requirement set out in point 67 of the R&R Guidelines is also met.

3.3.3.3. Avoidance of undue distortions of competition

(139) Pursuant to point 38 (f) of the R&R Guidelines, when restructuring aid is granted, measures must be taken to limit distortions of competition, so that adverse effects on trading conditions are minimised as much as possible and positive effects outweigh any adverse ones.

(140) As explained further in points 87 to 93 of the R&R Guidelines, the measures to limit competition distortions should be in proportion to the distortive effects of the aid, and in particular: (i) to the size and the nature of the aid and the conditions and circumstances under which it was granted; (ii) to the size and relative importance of the beneficiary in the market and the characteristics of the market concerned and (iii) to the extent to which moral hazard concerns remain following the application of the own contribution and burden-sharing measures. The structural measures might include divestment of assets, reducing capacity or market presence. They should favour the entry of new competitors, the expansion of existing small competitors or cross-border activity. Behavioural measures aim at ensuring that aid is used only to finance the restoration of long-term viability and that it is not abused to prolong serious and persistent market structure distortions or to shield the beneficiary from healthy competition.

(141) The restructuring plan includes three measures to limit competition distortion. First, as structural measure, the beneficiary will withdraw from the market for industrial solutions and liquidate the subsidiary Đuro Đaković Industrial Solutions. Đuro Đaković Industrial Solutions has been active in industrial solutions, both as a sole provider or has

often participated in different consortia comprised of other project engineering companies (domestic and foreign) providing services of projects engineering. As such, Đuro Đaković Industrial Solutions has had a track record of a profitable business. By exiting the market, this measure will allow domestic and foreign competitors to fill the gap (recital (72)).

(142) As a second measure, the beneficiary will commit not to extend its overall production capacity over the current level and keep output below full utilisation (1 200-1 400), at the level of 1 000 wagons a year for the duration of the restructuring plan (recital (73)).

(143) As a third measure, the beneficiary will discontinue production of three types of wagons, which have altogether an annual potential production of 300 pieces and turnover of EUR […] million. There is a very limited number of manufacturers that produce these wagon types, which are in demand. By discontinuing production of these, the beneficiary leaves a major spot on the niche market for other competitors to fill (recital (76)).

(144) When it comes to behavioural measures, as set out in recital (77) Đuro Đaković will refrain from acquiring shares in any company, during the restructuring period, except where it is indispensable to its long-term viability, subject to an authorisation by the Commission. Croatia has not indicated that such acquisitions of shares are envisaged nor is there any acquisition of shares in any company included in the restructuring plan of the beneficiary. Furthermore, Đuro Đaković commits not to publicise the restructuring aid as a competitive advantage.

(145) Based on the information provided, the Commission concludes that, overall, the measures already taken and those planned to limit distortions to competition, on the freight wagon and the industrial solution markets, are appropriate taken into account the limited size of the beneficiary both in terms of activity (turnover, staff, etc.) and position, including a market share below 5% on the EU market for freight wagons. These measures are adequate to compensate the distortions of competition caused by the restructuring aid and thus, comply with points 76 to 93 of the R&R Guidelines.

3.3.3.4. ‘One time, last time’ principle and other conditions

(146) According to point 71 of the R&R Guidelines, if an undertaking concerned has already received rescue or restructuring aid in the past, including any non-notified aid, and where less than 10 years have elapsed since the rescue aid was granted or the restructuring period came to an end or implementation of the restructuring plan has been halted (whichever occurred the latest), the Commission will not allow further rescue or restructuring aid. This is because repeated instances of restructuring aid supporting various failed restructuring plans are evidence that the restructuring plans did not secure a solid contribution of the beneficiary on a lasting and viable basis to the development and increased productivity of the economic activity that it performs. In the

meantime, by artificially maintaining in place a competitor which would otherwise exit the market, repeated restructuring aids distort competition with non-aided competitors, which cannot grow, take-over or expand within the internal market to an extent that is contrary to the common interest of the EU.

(147) Croatia informed the Commission that neither Đuro Đaković nor its shareholders have previously received any rescue aid, other than the one approved by the Commission in the rescue aid decision, or restructuring aid (recital (38)). The Commission has also verified in its records, which confirm the absence of previous approvals of rescue or restructuring aid for the undertakings in question, as well as of related complaints within the last ten years. Therefore, the planned restructuring aid to the undertaking complies with the '*one time, last time*' principle, as set out in point 70 and following of the R&R Guidelines.

(148) Furthermore, in keeping with points 94 and 96 of the R&R Guidelines, Croatia has informed that Đuro Đaković has not benefitted from previous State aid, which the Commission has declared to be illegal and which would not have been recovered, and that it plans to publish the aid granting decision and meet other transparency requirements on the following two websites:

www.mfin.gov.hr

www.mingor.gov.hr

(149) The Commission considers it necessary that Croatia provides biannual reports on the implementation of the restructuring plan every six months from the date of this decision until the end of the restructuring period set at until end of 2023. The Commission also recalls Đuro Đaković's obligation to implement the restructuring plan, as well as the measures limiting the distortions of competition. These reports will specify, in particular, the actual servicing and reimbursement of the restructuring aid, any deviations from the financial or operational trajectories of the restructuring plan and the corrective measures envisaged or taken by Đuro Đaković where appropriate.

3.3.3.5. Weighing up the positive effects of the aid with the negative effect on the internal market

(150) A carefully designed State aid measure must ensure that the overall balance of the effects of the measure is positive by avoiding altering trading conditions to an extent contrary to the common interest.

(151) In the R&R Guidelines, the Commission laid down the criteria that it examines when assessing the compatibility of restructuring aid with the internal market, ensuring that the development of the economic activities and/or areas which the aid seeks to support does not adversely affect trading conditions to an extent contrary to the common interest.

(152) In its assessment the Commission has taken into account the positive impact of the restructuring aid in supporting the development of the depressed region where Đuro Đaković is located, as well its systemic role as the sole domestic supplier of certain goods and services to the Croatian Ministry of Defence, pursuant to point 44(a) and (c) of the R & R Guidelines (Section 3.3.2.1).

(153) In particular, given the importance of Đuro Đaković for the area of Panonska Hrvatska (and notably the Brod-Posavina county) and its economic and social development, as described above, in the absence of aid, the economic growth and employment situation of that region would be seriously affected and would also likely involve serious social hardship. As referred in recitals (40) to (55), the new investor has presented an ambitious plan which foresees a cooperation and support from wider community, including suppliers and scientific community, local university, bringing young engineers on board, scholarship programmes etc., all of which will be developed on good examples that proved successful in the past and further strengthened by experience, programmes and supports the new investor has gained in other companies and regions.

(154) As regards the negative effects of the aid on competition and trade, the Commission found that the measures fulfil the conditions set out in the R&R Guidelines in that they are appropriate, necessary, proportionate, the respect the principles of 'one time, last time' and transparency, while being accompanied by commitments that further limit the negative effects of the measures on competition.

(155) In light of the above, the Commission concludes that the negative effects of the restructuring aid for the sector of the manufacturing of freight wagons, where the beneficiary will be mainly active post-restructuring, are limited. Consequently, the positive impact of the restructuring aid on the development of the economic areas and activities, identified in section 3.3.2., outweighs the potential negative effects on competition and trade, which are therefore not adversely affected to an extent contrary to the common interest.

3.4. Conclusion on compatibility

(156) In light of the findings above, the Commission has concluded that the measures fulfil all compatibility criteria of the R&R Guidelines and are therefore compatible with the internal market.

4. CONCLUSION

The Commission regrets that Croatia put the measures into effect, in breach of Article 108(3) of the Treaty on the Functioning of the European Union.

However, it has decided, on the basis of the foregoing assessment, not to raise objections to the aid on the grounds that it is compatible with the internal market pursuant to Article 107(3)(c) of the Treaty on the Functioning of the European Union.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://ec.europa.eu/competition/elojade/isef/index.cfm.

Your request should be sent electronically to the following address:

European Commission,
Directorate-General Competition
State Aid Greffe
B-1049 Brussels
Stateaidgreffe@ec.europa.eu

Yours faithfully,

For the Commission

Margrethe VESTAGER
Executive Vice-President