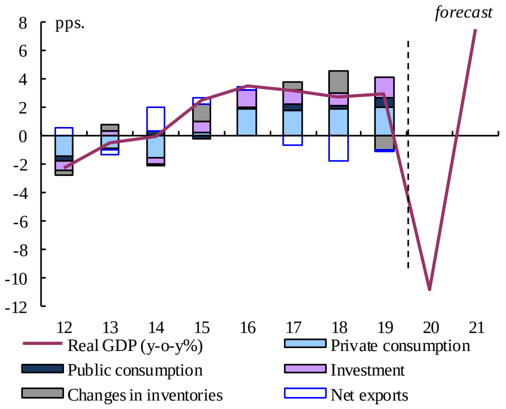
2.23. CROATIA

When the COVID-19 pandemic reached Croatia, the economy was in a more resilient position than it had been at the onset of the 2008 global financial crisis. Nevertheless, GDP growth turned negative in the first quarter (-1.2% q-o-q), as both domestic and external demand contracted, and is expected to have been even more negative in the second quarter. Available high frequency and sentiment indicators suggest that a trough in economic activity may have been reached in April and may be followed by a sharp recovery in May and June.

Overall, real GDP is expected to contract sharply in 2020 (close to 11%) and to partially recover in 2021, leaving output below its pre-crisis level. Domestic demand is expected to be the main driver of both the drop in GDP in the first half of 2020 and its recovery thereafter. Private consumption should recover quickly with the reopening of the economy, as large scale layoffs appear to have been avoided, thanks to the government's wage support measure. Ongoing and new projects financed by EU funds and several liquidity support measures for companies should facilitate recovery in investment. Croatia's sizeable tourism sector, accounting for the majority of services exports, is expected to remain depressed throughout 2020 and to only gradually recover in 2021, owing to remaining disruptions in international travel. Overall, exports are expected to take longer to recover, also given the worsened global outlook and uncertainties surrounding global trade.

Graph 2.23: **Croatia - Real GDP growth and contributions**



The HICP inflation rate picked up slightly in the first quarter of the year due to the dissipating effect of a VAT decrease on unprocessed food enacted in 2019. It has since turned negative, mainly on account of a significant decline in energy prices, which are expected to remain the main driver of inflation in 2020 and 2021. Food prices are also expected to positively contribute to inflation, but core inflation is expected to remain stable in both 2020 and 2021.