



2021 SME COUNTRY FACT SHEET'S BACKGROUND DOCUMENT

CROATIA

1. Introduction

Croatia is among the best performing countries in the EU in terms of internationalisation activities. While the regulatory burden still remains a challenge for small and medium-sized enterprises (SMEs), access to public financial support and changes to the tax system have helped them develop their businesses. Nevertheless, Croatian SMEs lag behind the EU average on business digitalisation and innovation as well as sustainability measures.

SMEs in Croatia were badly affected by the COVID-19 pandemic in 2020 and the policy measures taken to tackle it. The devastating earthquakes of March and December last year added to the negative impact. SME value added dropped sharply by 7.6% but SME employment declined only slightly by 0.4%¹, mostly thanks to the government support measures that cushioned the negative impact in the short term. The downturn was particularly pronounced in the *accommodation and food services* sector, where SME value added fell by 33.1% and SME employment by 8.4%, and in the *transportation and storage* sector, where SME value added declined by 15.4%, while SME employment remained static (0.1% growth). However, several sectors performed relatively well, such as the *construction* sector, where SME value added grew by 3.0% and SME employment by 1.6%.

A partial recovery of the economy is expected for 2021. SME value added is projected to increase by 5.7%, although this is still 2.4 % below its 2019 level². Meanwhile, SME employment is expected to level off (0.0% growth) and remain 0.4% below its 2019 level.

In 2020, Croatian SMEs accounted for 63.7% of value added and 67.4% of employment in the 'non-financial business economy', exceeding the respective EU averages of 53.0% and 65.3%. They employed an average of 4.6 people, exceeding the EU average of 3.7. However, the average productivity of Croatian SMEs, defined as value added per person employed, was EUR 20 600, approximately half the EU average of EUR 40 000.

Figure 1: Number of enterprises, persons employed and value added in 2020

	Number of enterprises			Number of persons employed			Value added		
	Croatia		EU-27	Croatia		EU-27	Croatia		EU-27
	Number	Share	Share	Number	Share	Share	€ billion	Share	Share
Micro	139 994	90.9%	93.3%	296 555	28.1%	29.6%	4.9	21.2%	18.7%
Small	11 661	7.6%	5.7%	225 915	21.4%	19.7%	5.3	23.3%	17%
Medium-sized	1 822	1.2%	0.9%	187 825	17.8%	15.8%	4.4	19.2%	17.3%
SMEs	153 477	99.7%	99.8%	710 295	67.4%	65.2%	14.6	63.7%	53%
Large	457	0.3%	0.2%	343 551	32.6%	34.8%	8.3	36.3%	47%
Total	153 934	100%	100%	1 053 846	100%	100%	22.9	100%	100%

source: These are estimates for 2020 produced by DIW Econ, based on 2008-2018 figures from the Structural Business Statistics Database as well as provisional data for 2019-2020 from the National Accounts Database and the Short-Term Business Statistics Database (Eurostat). The data cover the 'non-financial business economy', which includes industry, construction, trade, and services (NACE Rev. 2 sections B to J, L, M and N), but not enterprises in agriculture, forestry and fisheries and the largely non-market service sectors such as education and health. The following size-class definitions are applied: micro firms (0-9 persons employed), small firms (10-49 persons employed), medium-sized firms (50-249 persons employed), and large firms (250+ persons employed).

2. Key strengths

Changes to the Croatian tax system implemented in recent years are starting to show results

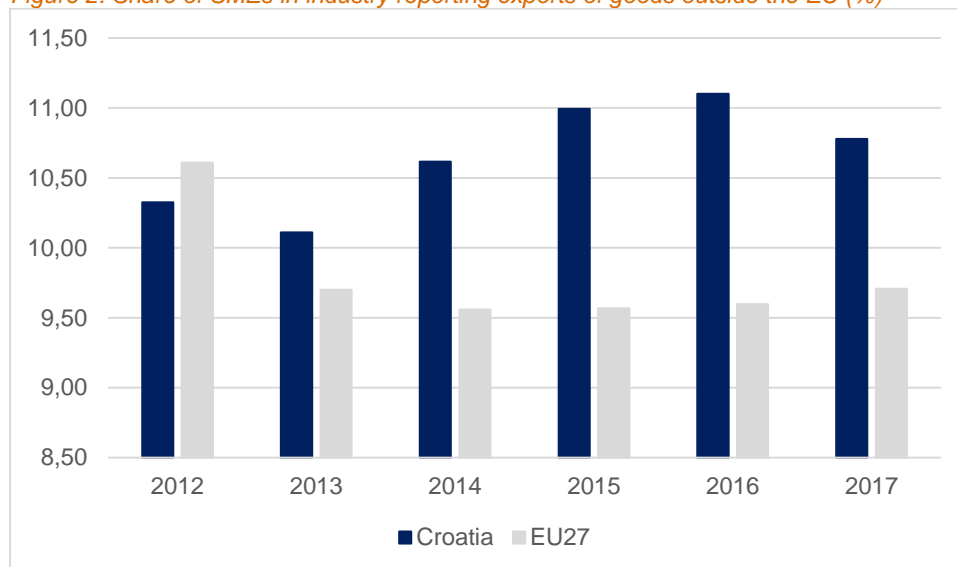
The country is among the top 50 best performers worldwide on the 'tax payment' criteria³ in the World Bank's Ease of Doing Business 2020 rankings, scoring 81.8 out of 100⁴. The score remained stable compared to 2019, when Croatia also scored 81.8. Its strong performance on this indicator reflects the government's focus on reforming the tax system in recent years through multiple amendments to different tax legislations. The main goal is to address SME needs.

2020 saw the government continue to improve the business environment as part of the national reform programme 2020 (*Unapređenje poslovnog okruženja u okviru Nacionalnog programa reformi 2020*). One of the measures, 'Improving the business environment', is particularly important for SMEs – it addresses their needs while also focusing on improving the quality of public governance and policies in order to stimulate economic growth and strengthen their competitiveness. This measure consists of three main areas of intervention. For SMEs, unbundling the administrative and parafiscal charges is the most important one, together with deregulating services further and stopping undeclared work. The government has drawn up two action plans to address these points: the 2020 action plan for administrative unbundling of the economy (*Akcijski plan za administrativno rasterećenje gospodarstva*) and the 2020 action plan for reduction of non-tax and parafiscal levies (*Akcijski plan za smanjenje neporeznih i parafiskalnih davanja*)^{5,6,7}. Efforts to improve the business environment, including plans to reduce the administrative burden and parafiscal charges and deregulate services further, are also part of Croatia's pre- and post-Exchange Rate Mechanism II entry commitments.

Croatia is one of the top EU countries on internationalisation

The country is among the best performing countries among EU countries in internationalisation activities⁸. It is also the top performer in 'trading across borders' according to the World Bank's Ease of Doing Business 2020 rankings⁹. The Flash Eurobarometer on SMEs, start-ups, scale-ups and entrepreneurship from 2020 indicates that 39% of Croatian SMEs export to other EU countries, which is significantly higher than the EU average of 23%¹⁰. In recent years, multiple governmental activities have focused on export-related measures, mainly in the forms of grants introduced by various ministries.

Figure 2: Share of SMEs in industry reporting exports of goods outside the EU (%)



Source: Eurostat, 2020¹¹

The country has achieved considerable success with a new venture capital fund

On access to public financial support, Croatia is among the best performers in the EU¹², with an upward trend evident in recent years. Recently, the joint project between the European Investment Fund, the Croatian Bank for Reconstruction and Development (HBOR) and the Croatian government established a new venture capital fund in Croatia (*Pokretanje novog fonda rizičnog kapitala*)¹³, supported by the European structural and investment funds. The fund consists of two major components: an accelerator programme dedicated to innovative start-ups, and equity investment for companies that are already operating. The amount of investment in an individual company depends on the level of development and ranges from EUR 10 000 through 'Start-up School' to EUR 1 million through equity investments.

In addition, HBOR has implemented three new loan programmes to make it easier to access working capital, encourage exports as well as encourage competitive export-driven entrepreneurs^{14,15,16}.

3. Key challenges

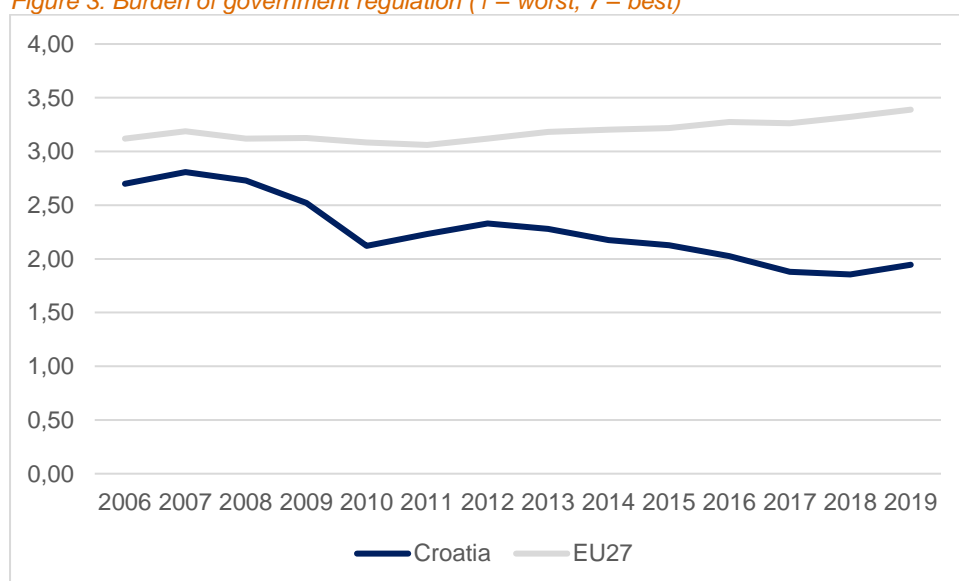
Regulatory burden has been decreasing but is still rather high

In 2016-2020, the country's position on government efficiency decreased slightly. It now ranks 59th in the International Institute for Management Development's World Competitiveness Ranking 2020¹⁷. The most revealing indicator for government efficiency is the business legislation criteria, where Croatia scores the worst²⁵. The country's business environment needs to be improved further, especially in the areas of administrative and parafiscal charges. Nevertheless, some improvements have been made in recent years, for instance through the national reform programmes implemented in 2019 and 2020 to improve the business environment (*Unapređenje poslovnog okruženja u okviru Nacionalnog programa reformi*). The services sector remains highly regulated in certain professions, although improvements have also been made by deregulating many professions and sectors (based on the OECD Product Market Regulation 2018 data).

In addition, when looking at the number of procedures needed to start a business, Croatia performs worse than the EU average, requiring 7 on average in 2020 against an EU average of 5.4¹⁸. Moreover, government agencies are not considered proficient and effective in supporting new and growing firms. The country also performed worse than the EU average in 2019 (on a scale of 1-5, 1 being the worst and 5 the best, Croatia scored 2.1 against an EU average of 2.8)¹⁹.

To tackle this issue, the government recently adopted the action plan for administrative unbundling of the economy as well as the action plan for reduction of non-tax and parafiscal levies^{20,21,22}.

Figure 3: Burden of government regulation (1 – worst, 7 – best)



Source: Global Competitiveness Report 2018-2019²³

The country lags behind the EU average on business digitalisation

The lack of financial resources is perceived to be the most significant barrier to digitalisation by Croatian SMEs. According to the Flash Eurobarometer on SMEs, start-ups, scale-ups and entrepreneurship from 2020, 24% of SMEs in Croatia think that a lack of financial resources is the limiting factor to further digitalisation of their activities, just above the EU average of 23%²⁴. In all six components of the 2020 Digital Economy and Society Index, Croatia scored below or close to the EU average, while it scored lowest on the digital public services indicator. Croatian SMEs

also lack sufficient skilled workers and ICT specialists²⁵. In 2018, ICT specialists accounted for a lower percentage of the workforce in Croatia compared to the EU average (3.5% against the EU average of 3.9%)²⁶.

There is a clear awareness in the business community of the needs for further digitalisation, and Croatian SMEs are open to digital transformation in general. Several measures have been implemented in recent years, but there is still a lack of human and financial capacity for digitalisation in SMEs.

The country scores below the EU average on sustainable business

On the sustainability measures taken, Croatian SMEs perform below the EU average on all eight categories according to the Flash Eurobarometer on SMEs, start-ups, scale-ups and entrepreneurship from 2020²⁷. In 2019, Croatia came 6th from last in the EU-28 eco-innovation ranking, scoring 25 points below the EU average. Croatian SMEs also perform below the EU average on the sustainability measures taken. In 2020, only 56% of them recycled or reused materials, below the EU average of 61%, and only 12% developed sustainable products or services, significantly below the EU average of 30%²⁸.

In the last decade, Croatia introduced a number of policy measures to address environmentally friendly business. Multiple measures were launched to stimulate renewable energy usage by offering financial support to SMEs, including support for environmental management certificates, but additional efforts are needed in the near future.

Croatia lags behind the EU average on innovation

As reported by the European Innovation Scoreboard 2020, Croatia is considered a moderate innovator and still performs below the EU average²⁹. However, it has made significant improvements since 2012. When looking at the two indicators on SME innovations in terms of products and processes and the number of SMEs innovating in-house, Croatia still performs slightly below the EU average, but the country now scores higher compared to the EU on SME marketing and organisational innovations³⁰.

Moreover, the government introduced policy measures in 2019 and 2020 to boost innovation. Examples include the Proof of Concept – PoC8 (*Provjera inovativnog koncepta – PoC8*) to support innovation at an early stage of research³¹ (2019), and the development of an entrepreneurial network (*Razvoj mreže poduzetničkih potpornih institucija putem HAMAG-BICRO – Faza 2*) to provide entrepreneurs with uniform access to business knowledge, skills, partners, information and services that are key to starting and developing a business³².

The government adopted a legal act on state aid for research and development projects in 2018, followed by an ordinance on state aid for research and development projects in 2019 so that companies (including SMEs) could apply for state aid. The act aims to increase private sector investment in R&D, increase the number of companies investing in R&D and encourage companies to collaborate with research and knowledge dissemination organisations on R&D projects. State aid can take the form of tax relief for R&D projects and feasibility studies (income tax base reduction).

While R&D expenditure as a percentage of GDP reached 2.19% for the EU on average in 2019, it only amounted to 1.11% in Croatia. This is the highest R&D expenditure as a percentage of GDP on record for Croatia. Nevertheless, the country still needs to make significant efforts.

4. Other key SME-related brief insights



IMPACT OF COVID-19 CRISIS ON SMES

The government adopted a new comprehensive national programme offering financial support to entrepreneurs affected by the COVID-19 crisis.

Liquidity and employment issues related to the COVID-19 crisis badly affected the country. According to the government, around EUR 1 billion (HRK 6.85 billion) has been paid so far for various measures to preserve jobs. With the written-off contributions added, the figure will be more than EUR 1.33 billion (HRK 10 billion).

The hardest hit sectors were sector H (*Transportation and storage*), I (*Accommodation and food services*) and M (*Professional, scientific and technical activities*)^{33,34,35,36}.



SCALE-UP ENVIRONMENT

The share of high-growth enterprises in 2017 (12.5% according to Eurostat data) was above the EU average of 11.5%. 2018 produced a similar trend, with Croatia also performing above the EU average (12.1% against 11.9% for the EU).

The employment share of high-growth enterprises (15.3% according to Eurostat data) was slightly below the EU average of 15.4%³⁷.



SOCIAL ASPECTS OF SUSTAINABILITY

Only 17% of SMEs engaged employees in governance in 2020, below the EU average of 49%³⁸.



START-UP ENVIRONMENT

The government adopted a new measure 'Development of the entrepreneurial support institutions network by Hamag Bicro' (Croatian Agency for SMEs, Innovations and Investments). The measure supports the development of an enhanced network of entrepreneurial support institutions that guarantees professional advisory and expert services to entrepreneurs.

¹ The data for 2020 are estimates produced by DIW Econ, based on 2008-2018 figures from the Structural Business Statistics Database as well as provisional data for 2019-2020 from the National Accounts Database and the Short-Term Business Statistics Database (Eurostat).

² Estimates for 2020 produced by DIW Econ, based on 2008-2018 figures from the Structural Business Statistics Database as well as provisional data for 2019-2020 from the National Accounts Database and the Short-Term Business Statistics Database (Eurostat).

³ The 'tax payment' criteria encompass four main indicators: the number of payments per year, the time required per year to prepare, file and pay taxes, the total tax and contribution rate (as a percentage of profit), and the postfiling index.

⁴ World Bank Group (2020), *Ease of doing business in Croatia*, available at:

<https://www.doingbusiness.org/en/data/exploreeconomies/croatia#>

⁵ Vlada Republike Hrvatske (2020), *Nacionalni program reformi 2020*, available at:

<https://vlada.gov.hr/UserDocsImages//2016/Sjednice/2020/Travanj/227%20sjednica%20VRH/Novi%20direktorij//227%20-%201.pdf>

⁶ Vlada Republike Hrvatske (2020), *Akcijski plan za administrativno rasterećenje gospodarstva 2020*, available at:

<https://vlada.gov.hr/UserDocsImages//2016/Sjednice/2020/Travanj/227%20sjednica%20VRH//227%20-%203%20Akcijski%20plan%20za%20administrativno%20rastere%C4%87enje%20gospodarstva%202020.docx>

⁷ Vlada Republike Hrvatske (2020), *Akcijski plan za smanjenje neporeznih i parafiskalnih davanja*, available at:

<https://vlada.gov.hr/UserDocsImages//2016/Sjednice/2020/Svibanj/229%20sjednica%20VRH//229%20-%206%20AP.docx>

⁸ European Commission (2019), *SBA Fact Sheet Croatia*, available at:

<https://ec.europa.eu/docsroom/documents/38662/attachments/5/translations/en/renditions/native>

⁹ See Note 4

¹⁰ European Commission (2020), *Flash Eurobarometer 486, SMEs, start-ups, scale-ups and entrepreneurship*, available at:

<https://ec.europa.eu/commfrontoffice/publicopinion/index.cfm/ResultDoc/download/DocumentKy/90710>

¹¹ Eurostat (2020), available at: <http://epp.eurostat.ec.europa.eu/newxtweb/setupdimselection.do>

¹² See Note 8.

¹³ Seenews (2019), *Croatia's first startup venture capital fund launches operations – report*, available at:

<https://seenews.com/news/croatias-first-startup-venture-capital-fund-launches-operations-report-661151>

¹⁴ Croatian Bank for Reconstruction and Development (HBOR), *Obrtna Sredstva*, available at:

https://www.hbor.hr/kreditni_program/obrtne-sredstva/

¹⁵ Croatian Bank for Reconstruction and Development (HBOR), *Investicije Privatnog Sektora*, available at:

https://www.hbor.hr/kreditni_program/investicije-privatnog-sektora/

¹⁶ Croatian Bank for Reconstruction and Development (HBOR), *Investicijski Krediti Za Ruralni Razvoj*, available at:

https://www.hbor.hr/kreditni_program/investicijski-krediti-za-ruralni-razvoj/

¹⁷ IMD World Competitiveness Center (2020), *World Competitiveness Rankings 2020 Results*, available at:

<https://www.imd.org/wcc/world-competitiveness-center-rankings/world-competitiveness-ranking-2020/>

¹⁸ World Bank Doing Business (2020), available at: <http://www.doingbusiness.org/>

¹⁹ Global Entrepreneurship Monitor (2019), *National Expert Survey of the Global Entrepreneurship Monitor*, available at:

<http://www.gemconsortium.org/>

²⁰ See Note 5.

²¹ See Note 6.

²² See Note 7.

²³ Global Competitiveness Report 2018-2019, available at:

http://www3.weforum.org/docs/GCR2018/GCI_4.0_2018_Dataset.xlsx

²⁴ See Note 10.

²⁵ European Commission (2020), *Digital Economy and Society Index (DESI) 2020*, available at:

<https://ec.europa.eu/digital-single-market/en/news/digital-economy-and-society-index-desi-2020>

²⁶ Ibid.

²⁷ See Note 10.

²⁸ European Commission (2019), *Eco-Innovation at the heart of European policies*, available at:

https://ec.europa.eu/environment/ecoap/croatia_en

²⁹ European Commission (2020), *European Innovation Scoreboard 2020*, available at:

https://ec.europa.eu/growth/industry/policy/innovation/scoreboards_en

³⁰ Ibid.

³¹ HAMAG BICRO (Croatian Agency for SMEs, Innovations and Investments) established by the Government of the Republic of Croatia, *Otvoren Javni poziv PoC8*, available at: <https://hamagbicro.hr/otvoren-javni-poziv-poc8/>

³² Bond, *Sto je Bond*, available at: <https://bond-hrvatska.hr/>

³³ Od mjere do karajere (2020), *Potpore za očuvanje radnih mjesta*, available at: <http://mjere.hr/mjere/potpore-ocuvanje-radnih-mjesta/>

³⁴ Od mjere do karajere (2020), *Potpore za očuvanje radnih mjesta*, available at: <http://mjere.hr/potpore-ocuvanje-radnih-mjesta-dokumentacija-obraci/>

³⁵ Koronavirus.hr (2020), *Nastavak mjera za očuvanje radnih mjesta*, available at: <https://www.koronavirus.hr/nastavak-mjera-za-ocuvanje-radnih-mjesta/834>

³⁶ Vlada Republike Hrvatske (2020), *Premijer o potporama za očuvanje radnih mjesta: Danas imamo više zaposlenih nego prije krize u veljači*, available at: <https://vlada.gov.hr/vijesti/premijer-o-potporama-za-ocuvanje-radnih-mjesta-danas-imamo-vise-zaposlenih-nego-prije-krize-u-veljaci/29875>

³⁷ Eurostat (2020), *High growth enterprises (growth by 10% or more) and related employment by NACE Rev. 2*, available at: http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=bd_9pm_r2&lang=en

³⁸ See Note 10.