



REPUBLIC OF CROATIA

MINISTRY OF FINANCE

A N N U A L R E P O R T

OF THE MINISTRY OF FINANCE

1998

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A Word from the Minister of Finance



The limits to conducting fiscal policy in 1998 were determined by the international financial crisis and the introduction of the value-added tax, which concluded the reform of the fiscal system. After long and extensive preparations, the value-added tax with a flat rate of 22 percent was introduced on 1 January 1998. Although just before its introduction a negative atmosphere was created among the public, today we can say that the introduction of the value-added tax was a success. The value-added tax has proved itself to be anti-inflationary, causing only a single jump in prices in January 1998, after which prices returned to the customary monthly dynamics. Prices in December 1998 were 5.4 percent greater than in December 1997, of which 2.4 percent can be considered a consequence of introducing the value-added tax. This shows that the price trends established after the introduction of the stabilisation program were maintained in 1998. The strongest argument proving this assertion is the price trend in the first four months of 1999, when an inflation rate of 3.4 percent was recorded.

The value-added tax has proven itself as a considerably more effective generator of central budgetary revenues than the former sales tax. In 1998, revenues generated by the value-added tax were approximately HRK 5 billion more than those planned in the 1998 budget. Since the value-added tax rate is less than the standard rate of the former sales tax, it is clear that the introduction of the value-added tax did not cause an increase in the tax burden on consumption. What did occur, and this led to considerably greater revenues than expected, was the exceptional enhancement of tax discipline made possible by the self-control mechanism built into the credit method system of calculating the value-added tax.

The international financial crisis made access to the international capital market impossible for Croatia under favourable conditions, which is why the year ended with a fiscal surplus. It is precisely such an outcome that once more showed the flexibility of fiscal policy and its ability to adapt to the circumstances of its environment. Namely, over the past five years (with the exception of 1995, when Operations Flash and Storm were staged to liberate a part of the state's territory) the central state budget was successful in generating considerably lower deficits than planned in these years. Such results were achieved during a period in which there was a multiple reduction of tax rates for various tax forms, while outlays for the renewal of areas destroyed by the war, as well as outlays earmarked for transfers to extra-budgetary funds continued to grow. Moreover, in 1998 the children's allowance and water utility contributions were discontinued, which set off the process of reducing labour costs while the financing of these functions was completely assumed by the central budget.

However, 1998 was also a year in which it became apparent that the greatest source of pressure on the growth of the public sector, as well as its deficit, could be found in the sphere of extra-budgetary funds. The stabilisation of the situation in extra-budgetary funds, primarily the Croatian Pension Insurance Institute and the Croatian Health Insurance Institute, is the principal goal of fiscal policy in 1999. It is completely clear that the commenced reform of the pension system will secure a fiscally sustainable pension insurance system. However, it is equally clear that over the coming mid-term period, the central budget will have to transfer considerable funds into the so-called pay-as-you-go "first pillar," both because of the large number of existing pensioners and because of their age structure. However, the very fact that the reform of the system has commenced shows that in the sphere of pension insurance we are at the beginning of a period when this problem will finally be resolved. However, a thorough reform of the health-care financing system still awaits us.

All of the accomplishments achieved by the Ministry of Finance in the preceding period are the result of the persistent and dedicated work of my predecessors who held the post of finance minister and all employees of the Ministry of Finance. Therefore, I would like to thank all of my co-workers, just as all employees of the Ministry of Finance, for their efforts and support.

Zagreb, 25 May 1999

Borislav Škegjo



*Deputy Prime Minister and
Minister of finance*

I. MACROECONOMIC TRENDS IN 1998

1. EXTERNAL SITUATION

As in all other transition economies, the Croatian economy has functioned under the conditions of the unstable international financial market during the last two years. The financial crisis has spread from Asian markets to almost all emerging markets, leading to an increased insecurity and lack of investor confidence, so that interest returned to the markets of developed countries. The cost of capital for emerging markets, including Croatia, has increased considerably. Although the Asian crisis did not have a direct influence on the transition countries of Central and Eastern Europe, the negative perception of investors and increased sensibility to risk in the second half of the year have resulted in decreased capital investments of foreign investors in transition countries.

The introduction of a single European currency was definitely an event which marked the end of 1998 and the beginning of 1999. The European Central Bank fixed the exchange rate of the Euro in accordance with the currencies of the European Monetary Union member states on New Year's Eve and thus opened a new chapter in history. The unification of eleven European countries and the introduction of the single currency should increase market liquidity, cancel foreign exchange risk and reduce transaction-operating expenses in the euro zone. In the period immediately following its introduction, the Euro gained strength in relation to the dollar, and at a certain point it reached a price of US\$ 1.18, partly due to the Brazilian crisis. However, soon after the successful launching of the Euro, the recessionary indicators of the European economy cut the value of the Euro down to US\$ 1.08.

1999 forecasts on the basic macroeconomic indicators of developed countries have changed considerably in the last few months to the benefit of higher growth rates of the American economy and the decreased growth rates in European countries. The 1999 forecast of growth of the American economy been increased to 2.8 percent, while the forecast of growth for the Euro zone has decreased to 1.8 percent. A reduction of interest rates in European countries in December 1998, aimed at balancing the referential interest rates to about 3 percent, will have a significant influence on the European economy only in the second half of this year.

The Russian crisis commenced with the collapse of the Russian currency in August 1998. The stock markets reacted immediately with a stock price declines at double digit rates. The trade exposure of more advanced transition countries compared to the Russian market is low (about 4 percent of total goods exports on the average, except for Poland), so that there was no greater impact on the balance-of-payments current account. Increased pressure came from Western European countries, where economic growth slowed down and the growth rate of real domestic demand decreased. The EBRD has estimated that a decrease of Western European import demand by only 2 percent could result in decreased growth in real terms of more advanced transition countries by 0.5 to 1 percent. The Russian crisis has revealed weaknesses in most transition countries in basic macroeconomic indicators and additionally pointed to a lack of structural reforms. Investor confidence can be successfully returned only if transition countries make steps to reduce government spending, reduce external imbalances and accelerate structural reforms.

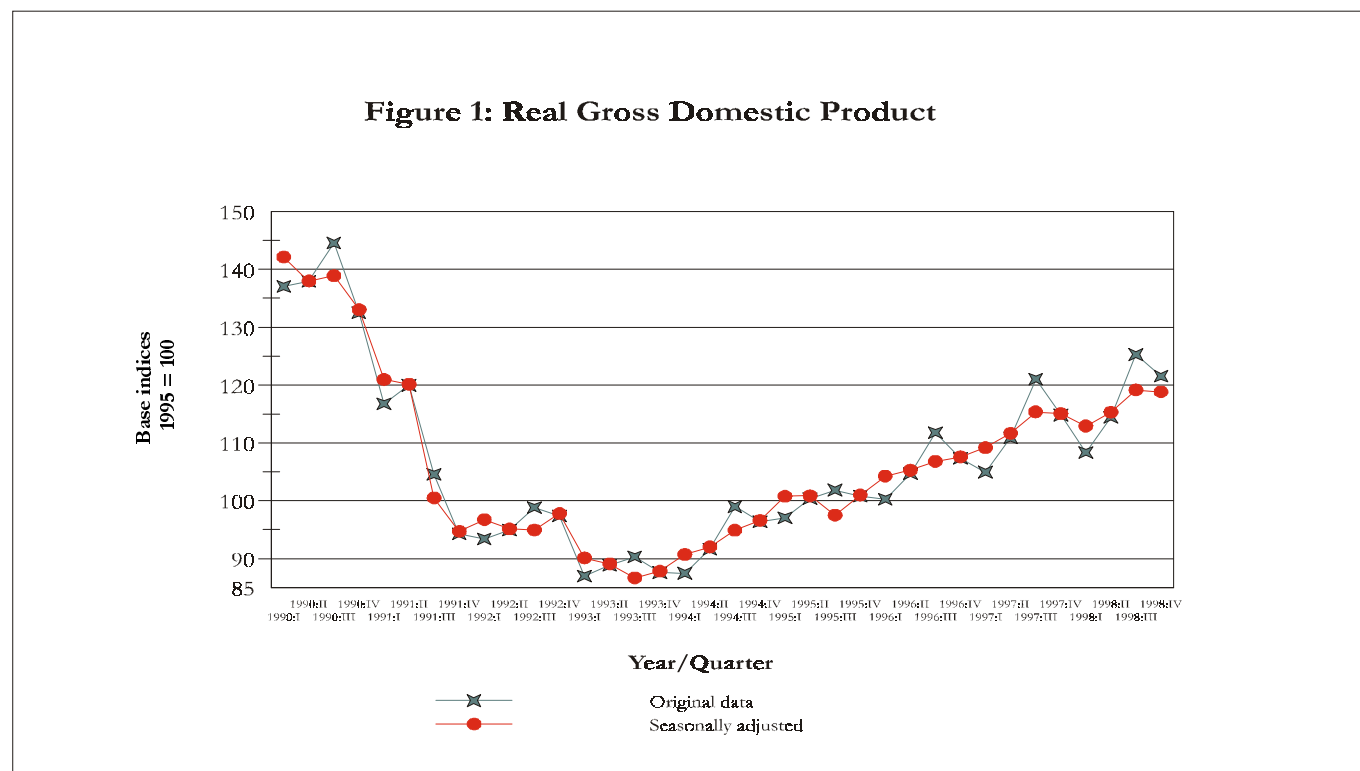
Table 1: Growth and Inflation in Countries in Transition

(percent change)	1997 (estimate)	1998 (forecast)	1999 (forecast)
Real GDP			
- Czech Republic	10.0	-1.0	2.5
- Croatia	6.5	4.2	3.7
- Hungary	4.4	4.6	4.9
- Poland	6.9	5.2	5.6
- Slovak Republic	6.5	5.0	3.3
- Slovenia	3.8	4.0	4.5
Inflation			
- Czech Republic	10.0	9.0	9.0
- Croatia	3.8	6.0	5.7
- Hungary	18.4	13.5	12.2
- Poland	13.2	10.0	9.9
- Slovak Republic	6.4	9.0	8.3
- Slovenia	8.8	7.0	9.0

Source: "Transition Report 1998", EBRD, 1998

2. THE REAL SECTOR

The Croatian economy achieved an average annual growth rate of over 6 percent in the period from 1994 to 1997. Such high rates of growth in real terms were achieved under conditions of stable trends in prices and exchange rates, growth in the standard of living and considerable growth of savings. However, preliminary estimates of the growth rates in real terms in 1998 are about 3 percent. The economic growth slowdown has been transferred from 1998 to 1999, and it will have to influence the growth rate in 1999. Figure 1 presents a quarterly trend of gross domestic product (GDP) and the strong seasonality of the third and fourth quarters can be clearly observed.



Source: Central Bureau of Statistics

Preliminary data on 1998 economic growth have been derived on the basis of only several analysed statistical indicators for all of last year. These estimates will change depending on the velocity of final annual data processing and bring them into line with other methods of GDP calculation. Namely, it should be mentioned that the growth rates for 1996 and 1997 are still provisional.

The results of surveys carried out on household consumption and income will be published for the first time after more than ten years. This will change both the structure and the size of official GDP, following the preliminary results¹. Although co-ordinated with the SNA methodology, such GDP size still does not include any estimates of the unofficial economy, and thus it can be concluded logically that the official GDP size has been significantly underestimated.

The Finance Ministry pointed to the underestimated official data on GDP size already at the beginning of last year. Namely, with the introduction of the value-added tax at the beginning of 1998, a significant part of the unofficial economy was encompassed, so that by the middle of the year it was clear that planned revenues from the value-added tax would be larger than projected in the budget. Empirical and theoretical notions of the relation between the VAT as a tax on consumption and aggregate economic activities show that none of the countries, adopting the VAT, collects more than 10 percent of the GDP from this type of tax. Since there is little possibility that the value-added tax eliminates tax evasion completely, and since the Croatian tax administration is the most efficient among the observed countries, there are arguments in favour of the claim that the official statistical data underestimate GDP size. With all possible limitations and particularities of the Croatian economy (consumption size in Croatia is about 10 percent higher than in developed countries with a

¹ According to preliminary results, real personal consumption is about 20 billion larger than the data available to official statistics so far.

single VAT rate; the amount of advance payment for the next accounting period and tax refunds should be deducted from potential VAT revenues, etc.), a regression analysis determined that GDP size in 1998 should be approximately HRK 180 billion, or approximately HRK 40 billion higher than official statistical estimates.

Trend indicators in the most important sectors which generate added value, as well as available financial indicators of entrepreneurial operations (according to the Institute of Payments (ZAP) data) are shown in Table 2. Revenues from the regular operations of legal persons in the economy have recorded a significant nominal growth rate of 13.7 percent in 1998 as well, or about 7.5 percent in real terms. Real indicators according to economic sectors indicate a significantly lower growth rate.

Table 2: Growth indicators

(growth rate, %)	1995/ 1994	1996/ 1995	1997/ 1996	1998/ 1997
Real GDP	6.8	6.0	6.5	2.7*
Revenue on ordinary activities (legal entities)	13.6	11.0	16.7	13.7
Industrial production total volume	0.3	3.1	6.8	3.7
Construction projects total volume	-3.9	9.0	16.9	2.4 (I-X)
Value of construction projects put in place (nominal)	19.5	45.3	33.2	15.0 (I-IX)
Retail turnover (real)	14.1	2.3	13.8	-0.4
Nights spent by tourists	-35.5	66.5	41.3	3.2
Income from tourist's services in USD	-25.0	49.1	25.6	7.8
Passengers carried	2.9	2.5	2.0	-6.7
Goods carried	20.2	0.0	1.5	-1.2

Source: Central Bureau of Statistics, Institute of Payments, Croatian National Bank

* preliminary data

Industrial output

Industrial output has been growing for four years now. After growth of 3.1 percent in 1996 and 6.8 percent in 1997, the physical volume of industrial output recorded growth in 1998 as well. The physical volume of industrial output increased by 3.7 percent in 1998 or 3.8 percent after the elimination of seasonal influence (seasonally adjusted to 1990 average). Output growth in the first eight months accounted for 6.9 percent, followed by a gradual monthly decrease of the industrial output index. The reasons for the decrease should be sought in the previously described aggravating possibilities for borrowing in the domestic and foreign markets, the high cost of capital, difficulties in collecting outstanding debts, decreased growth rates of domestic demand, and a lack of higher tourist consumption. The contraction of liquidity and the decrease of solvent demand in the domestic market have influenced a decline in imports, but also an increase in inventories and decrease of industrial output.

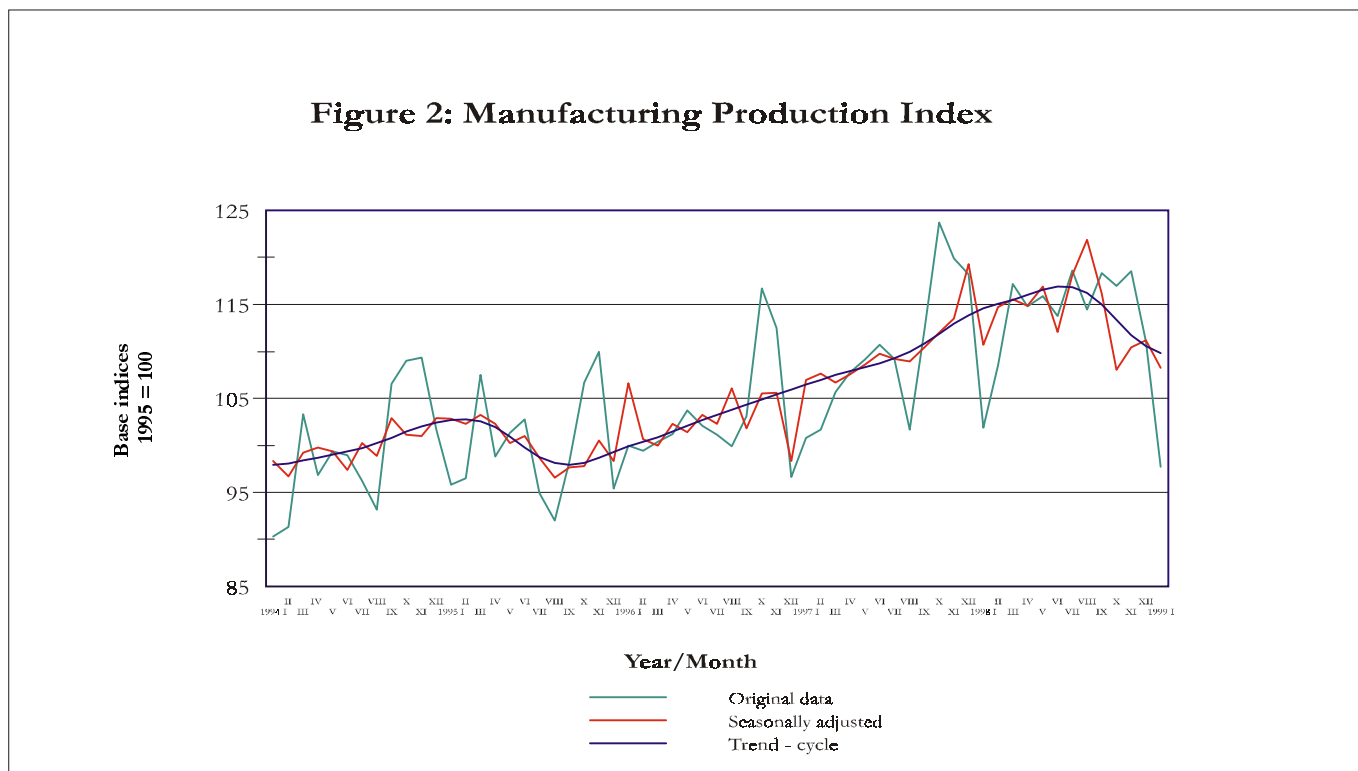
According to the National Classification of Activities, production growth of 8.7 percent was recorded last year in the production of electrical energy, natural gas and the water supply industry, 3.2 percent in the processing industry (accounting for 84.94 percent in the structure of the overall industrial output), while a decrease of 2.4 percent was recorded in mining and crude oil and natural gas extraction.

Table 3: Industrial production, stock of finished goods and exports (growth rate in 1998)

(in %)	Industrial production	Stock of finished goods	Export of goods (USD)
INDUSTRIAL PRODUCTION TOTAL	3.7	4.5	8.9
Mining and quarrying	-2.4	15.9	-72.4
Electricity, gas and water supply	8.7	-	2.7
Manufacturing	3.2	4.2	10.3
- Manufacture of food products and beverages	3.9	14.7	-3.8
- Manufacture of chemicals and chemicals products	-6.6	9.1	-4.6
- Publishing and printing	12.5	8.8	118.5
- Manufacture of fabricated metal products	11.1	8.1	3.3
- Manufacture of wearing apparel	-0.3	-9.0	0.8
- Manufacture of other non-metallic mineral products	14.0	52.6	-1.8
- Manufacture of other transport equipment	20.6	-13.9	348.7
- Manufacture of furniture	-5.4	-3.9	-13.1

Source: Central Bureau of Statistics

Production growth was recorded in twelve out of twenty-three sectors of processing industry in 1998. Last year the largest growth within the processing industry was recorded in the production of other means of transportation, or the shipbuilding industry, the production of which increased by 20.6 percent. A significant increase in production last year was also recorded in the production of metals (16.9 percent), medical and other precision instruments (16 percent), electric motors and appliances (15.4 percent), the production of other non-metal mineral products (14 percent) as well as publishing and printings activities (12.5 percent). The production of food and beverages, as the most important branch of the processing industry, recorded growth of only 3.9 percent, while the production of chemicals and chemical products was 6.6 percent lower than in the previous year.



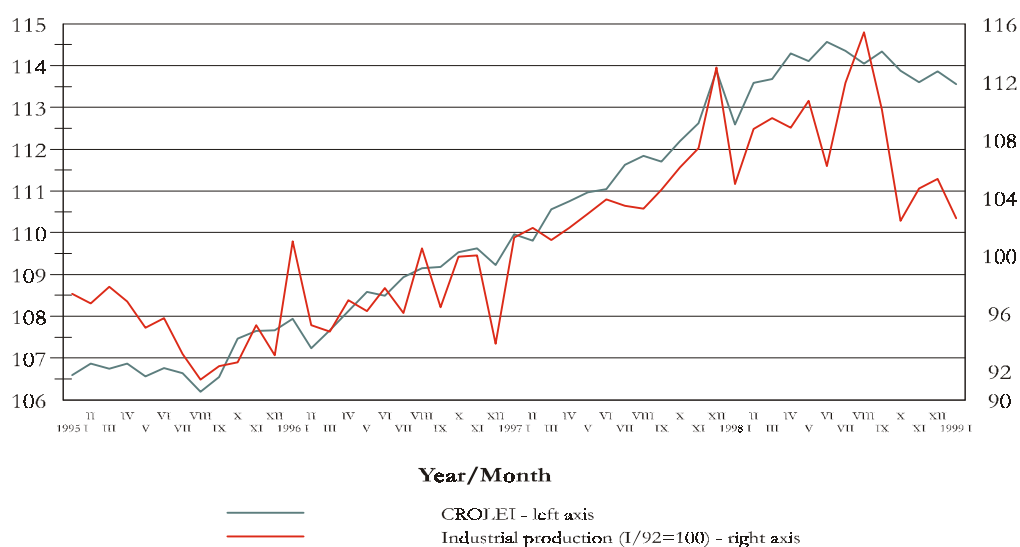
Source: Central Bureau of Statistics

Decrease in demand during the last year can be seen clearly in the increase of finished product inventories. Namely, finished industrial product inventories were 4.5 percent higher on average in 1998 than in 1997. A significant increase of inventories occurred already in August last year when a production decline began. Indications of positive trends were recorded in December of last year and January of this year when a certain decrease of inventories was recorded (by 2.7 percent in December compared to November and by 1.5 percent in January compared to December). The indications did not continue in February 1999, so that a significant recovery of industrial output is uncertain.

Figure 3 presents the preceding industrial output indicator or the CROLEI index². Already in August, the CROLEI index indicated the recessionary trends that would appear by the end of last and the beginning of this year. Namely, a negative production trend by the end of last year was transferred to January 1999. Overall industrial output was 4.1 percent lower in January 1999 than in January 1998, while non-seasonal data showed a decrease of 2.2 percent in January. The processing industry was reduced by 8.8 percent, and electrical energy supply increased by 20.4 percent. Production growth in January was achieved by only seven processing industry sectors. The latest CROLEI index observation in January 1999 does not indicate the possible recovery of industrial output at the beginning of the second quarter of this year.

²With the use of so-called leading indicators, the Economic Institute of Zagreb and the Finance Ministry have elaborated a complex forecast index **CROLEI (Croatian Leading Economic Indicator)**, according to the established method of the American National Bureau of Economic Research. The indicator announces a trend in industrial output and overall economic activity in Croatia, using the industrial output index for now as a reference series. The CROLEI index reflects a trend of the ten best leading indicators: *realised manpower requirements per month, unemployment allowance beneficiaries, the number of workers on construction sites, the number of tourist bed-nights - total, inventories in retail stores, unconsolidated state, county and municipal budget revenues, net wage budget - total, total liquid assets M4, placements.*

Figure 3: Leading Indicator of Industrial Production - CROLEI



Source: "Monthly statistical review of the Ministry of Finance"

Construction Industry

A growth trend has been observed in the construction industry as well for the third year in succession, although by significantly lower rates in 1998. The quantitative growth indicator of the construction industry measured by executed effective working hours increased by 16.9 percent in 1997, while the value of executed construction projects increased by 33.2 percent. In 1998 the sector's positive growth trend of the previous year was continued. The growth of the physical volume of construction projects accounted for 2.4 percent in the first ten months of 1998, while the value of executed construction projects was 15 percent higher in the first three quarters compared to the same period of the previous year. The aforementioned indicators, as well as the trends in state capital transfers for intensive reconstruction processes indicate that the construction industry will be a significant generator of growth in overall added value this year as well.

Due to the intensive reconstruction process of the areas destroyed during the war, construction is under the significant influence of capital investments by the state. If, as announced, the 1999 budget is re-balanced and capital expenditures reduced, this could have significant negative consequences for the construction industry in 1999.

Tourism

Trends in the tourism sector measured by the number of tourist bed-nights indicate continuous growth since 1996. The increase in the number of bed-nights accounted for 66.5 percent in 1996, 41.3 percent in 1997, while an increase of only 3.2 percent was recorded in 1998. The number of 5.4 million tourists increased by 4.7 percent compared to last year, resulting in 6 bed-nights per tourist on average. However, this quantitative measure does not reflect this sector's real contribution to overall added value. One of the possible value indicators is the trend of foreign currency inflow from tourist services, which was 49.1 percent higher in 1996 than in 1995 - gross tourism income accounted for US\$ 2.01 billion. The growth rate of tourism income accounted for 25.6 percent in 1997 compared to 7.8 percent in 1998, and gross tourism revenues amounted to US\$ 2.73 billion.

The most frequent guests on the Croatian coast are tourists from Austria, Germany, Italy, the Czech Republic, Slovenia and Bosnia-Herzegovina. Tourist perceptions of the political risk in Croatia and political events in neighbouring countries have a significant influence on their interest in the Croatian coast.

Therefore, the first estimates of bed-night growth of 10-12 percent in 1999 will probably not be realised considering current wartime hostilities in a neighbouring country.

Trade

The volume of retail trade, accounting for as much as 19 percent of GDP in 1996, indicates a growth in real terms since 1994 until last year. After growth in real terms of 14.9 percent in 1997, the volume of retail trade showed a decline in real terms of 0.4 percent in 1998. Retail trade turnover volume was 3.7 percent higher nominally than in the same period in 1997. A lower real growth of salaries and pensions in 1998 compared to 1997 as well as negative expectations have directed the population from consumption to savings, particularly in foreign currency, which is also indicated by Croatian National Bank data on increases in citizen foreign currency deposits.

3. PRICES AND THE EXCHANGE RATE

Prices

After the Stabilisation Program introduced in October 1993, average annual inflation, measured by retail prices, has remained at levels below 4 percent. The exception was in 1998 when inflation was 5.7 percent due to the introduction of the value-added tax. One of the most frequently asked questions regarding the introduction of the VAT to the tax system of the Republic of Croatia was its influence on the growth of prices and the possible subsequent tendency of an inflationary spiral. A year after the introduction of the VAT to the tax system of the Republic of Croatia, it can be concluded that its introduction was successful even from the aspect of price trends.

Table 4: Prices and cost of living

	1995	1996	1997	1998	I - II 1999
Retail prices, average, %	2.0	3.5	3.6	5.7	3.4
Producer's prices, average, %	0.7	1.4	2.3	-1.2	-0.5
Cost of living, average, %	4.0	4.3	4.1	6.4	3.2

Source: Central Bureau of Statistics

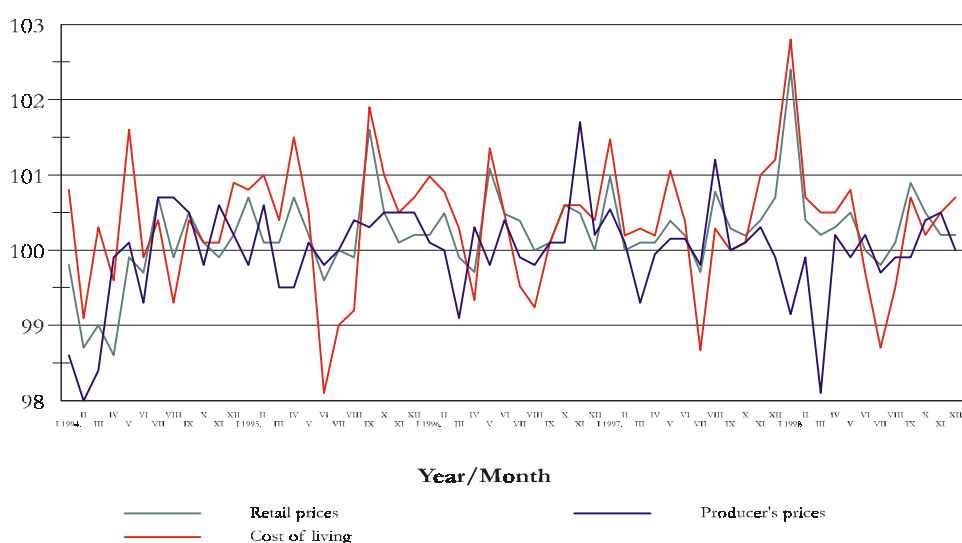
Monthly trends in the retail price index and the cost of living index indicate that during 1998 the VAT caused an expected one-off increase of prices by 2.4 percent in January, and after that price trends returned to their usual monthly dynamics. This effect could have been less if the possibility of price reduction had been completely utilised in relation to products for which the 22 percent VAT meant a reduction of the tax rate. Namely, with the introduction of the VAT, the standard rate was reduced from 26.5 percent to 22 percent. A certain effect to the fall of prices after the introduction of the VAT should have been provided by the cancellation of the sales tax from the expenses of economic subjects, or a cancellation of the so-called cumulative effect which accounted for 4.6 percent on average according to the estimates of the Finance Ministry and the International Monetary Fund. A recorded decline of industrial product prices by 1.2 percent in 1998 speaks on behalf of this conclusion. They were 2.1 percent lower in December 1998 than in December 1997. However, these tendencies in producer prices have not been transferred to final consumers, which can be seen in retail price indicators.

A retail price increase of 5.7 percent in 1998 was mostly due to a service price increase of as much as 12.1 percent, out of which the prices of housing and utilities increased the most, by 23.1 percent. Their increase was partly the result of the implementation of the Utilities Act, but also of their monopolistic position at the local and regional level. Last year the prices of postal and telecommunications services increased by 18.1 percent on average, professional/technical services by 14.5 percent and trade services by 13.7 percent.

Among the prices of goods which increased by 4.1 percent (including seasonal products), the prices of non-seasonal agricultural products and processed foodstuffs increased the most. The described trends are the result of an increase of food product prices by a percentage which corresponds approximately to the difference between the sales tax rate (15.5 percent for food products, and 10 percent for services) and the VAT rate (22 percent). At the same time, room for a decline in prices by 3.7 percent was possible due to a decrease in the tax rate for all products that were taxed by a standard rate (26.5 percent) according to the old tax system. However, the data show that the level of price decline is lower than the level of tax rate decrease, pointing clearly to the rigidity of prices in a downward direction.

Price trends during 1998 have shown again in practice that the tax is neither the only nor even a crucial determinant of price trends. The objectives and quality of business policy and market position are obviously much stronger determinants of trends in prices than the consumption tax such as the VAT. If a one-off price increase by 2.4 percent is deducted from the overall increase of prices in 1998, it can be noted that inflation was about 3 percent in 1998, and this is in accordance with the trends of previous years. A price increase of 3.1 percent in January 1999 confirms this estimate. The announcements of monetary and fiscal policy for 1999 are directed towards the maintenance of inflation at a level of 4 percent annually.

Figure 4: Monthly rates of change of retail prices, producer's prices and cost of living



Source: Central Bureau of Statistics

Table 5: Prices and cost of living in 1998

	XII 1998/ XII 1997	I - XII 1998/ I - XII 1997
Retail prices	105.4	105.7
- Goods	104.3	104.1
- Services	109.2	112.1
Cost of living	105.3	106.4
Goods	104.6	105.2
- Food	105.0	106.8
- Tobacco and beverages	100.2	99.2
- Clothing and footwear	105.6	105.8
- Housing	103.4	106.8
- Hygiene and health	106.1	108.8
- Education, culture and entertainment	114.4	113.6
- Transport and communication	111.9	112.4
Services	109.1	112.9
Producer's prices	97.9	98.8
Energy	91.4	93.5
Intermediate goods	97.4	97.2
Capital goods	101.9	102.5
Durable consumer goods	97.9	98.4
Non-durable consumer goods	100.4	101.3

Source: Central Bureau of Statistics

Exchange Rate

Since the introduction of the Stabilisation Program, the average monthly kuna exchange rate against the German mark, having the characteristics of a "managed floating" exchange rate, has stayed within relatively narrow limits. During the last five years, the average monthly DM exchange rate went from HRK 3.89 for DM 1 at most in March 1999 to the lowest level of HRK 3.51 for DM 1 achieved in January 1998, which is a difference of 10.8 percent. The DM exchange rate oscillates within these limits mainly because of the seasonal character of the balance-of-payments current account. Until 1998 the Croatian National Bank was often faced with the need to prevent excessive appreciation of the exchange rate.

Table 6: Exchange rate of HRK

	1995	1996	1997	1998	I - II 1999
Exchange rate HRK/USD, average	5.230	5.433	6.157	6.362	6.495
Exchange rate HRK/USD, end period	5.316	5.540	6.303	6.248	6.869
Exchange rate HRK/DEM, average	3.649	3.615	3.556	3.619	3.790
Exchange rate HRK/DEM, end period	3.706	3.562	3.511	3.740	3.870

Source: Croatian National Bank

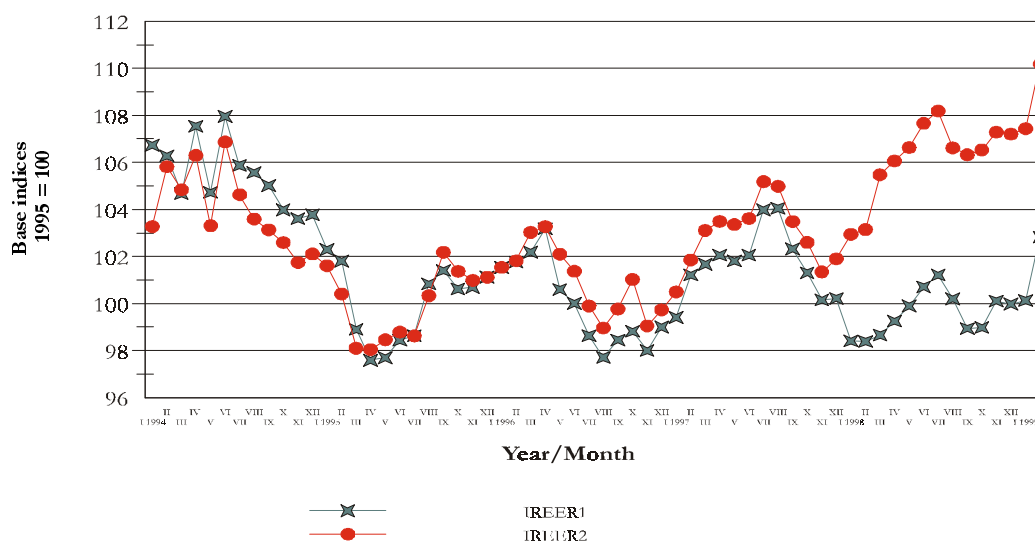
A stronger depreciation of the kuna against the German mark in the last few months has been caused by increased demand for foreign currency because of due dates for foreign loan repayment as well as due dates for import credits with relatively lower foreign currency inflows than during previous years. In the period from September to December, the kuna was devalued against the German mark by about 4 percent, and the pressure continued in January when the nominal depreciation accounted for 1.0 percent. The exchange rate level in January 1999 was 7.3 percent higher nominally than the level of the same period last year. This meant a depreciation of the real exchange rate along with slower price growth in the same period. Kuna depreciation in January was of a seasonal character and it has been recorded every year since the introduction of the Stabilisation Program.

The trends in the nominal effective exchange rate indicate a depreciation of 2.3 percent in 1998, which is less than in 1997 when the nominal effective exchange rate was depreciated by 3.4 percent. The effective exchange rate deflated by retail prices indicates that after a real depreciation of approximately 1.7 percent in 1997, the real effective exchange rate appreciated by 2 percent in 1998. A deflation of the effective exchange rate by producer prices points to a stronger depreciation of 3.1 percent in 1998 compared to 1.9 percent in 1997.

Domestic currency speculation and the creation of the so-called long position in German marks have resisted even the stronger sterilisation of central bank funds in the foreign currency market. A more significant foreign currency inflow of EURO 300 million in March, the amount of issued government bonds, has stabilised the exchange rate trend. The summer period will again put pressure on the appreciation of the Croatian currency against the German mark because of stronger seasonal foreign currency inflow, and also because of the sale of part of Croatian Telecommunications to foreign investors. The latter project should be implemented in the autumn of 1999.

Although the exchange rate was stabilised by the middle of March, the Croatian National Bank introduced additional monetary policy measures as protection against the possible continuation of speculative trends. The legal reserves of banks and savings banks have increased from 29.5 to 30.5 percent, and the central bank's interest rate on lombard loans has been increased from 12 to 13 percent. According to the Croatian National Bank, banks have financed the speculative demand for foreign currencies with a surplus of liquid funds above the real needs of financing import and servicing foreign currency loans.

**Figure 5: Index of Real Effective Exchange Rate of Croatian Kuna
(IREER1 - with retail prices, IREER2 - with producer's prices)**



Source: Croatian National Bank

4. LABOUR MARKET TRENDS

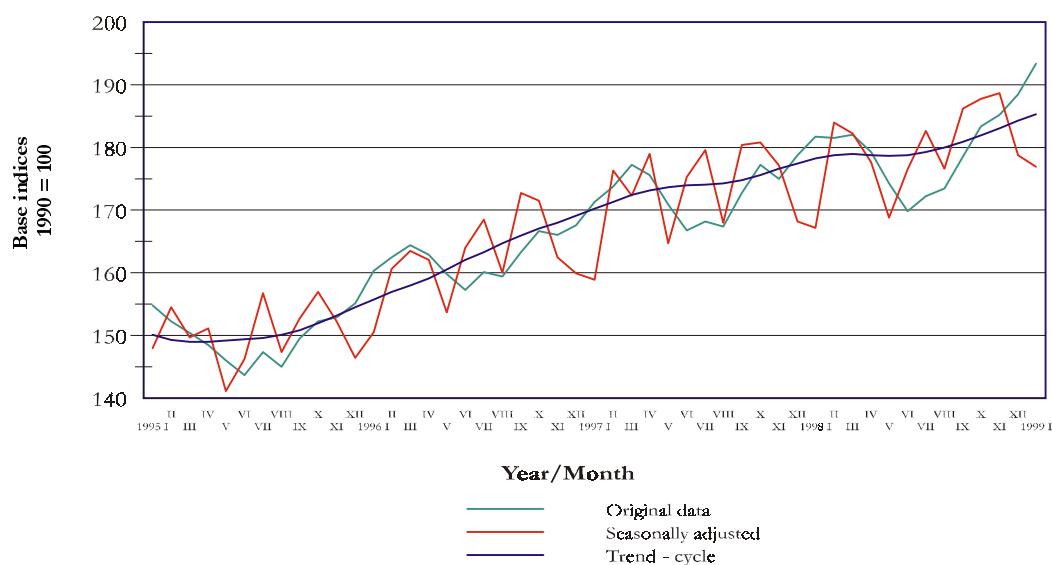
Employment and unemployment

During the last few years unemployment has increased as a result of the demobilisation of military forces, but also of the restructuring of former socially-owned companies. The velocity of surplus manpower absorption depended on private sector development, as well as on direct foreign investment, which was at an extremely low level in Croatia until 1998. For the first time in the post-war period, a positive shift has been noticed in employment data, which was 3.0 percent higher in 1998 compared to the average number of employees in 1997, according to the State Bureau of Statistics. However, the average number of the unemployed was 3.6 percent higher. According to the State Bureau of Statistics, the overall rate of unemployment accounted for 17.5 percent in 1997, and 17.6 percent annually in 1998, or 18.6 percent in December 1998. The structure of the unemployed in 1998 indicates that over 30 percent of the total number of unemployed are persons seeking employment for the first time.

The total number of employed persons includes those employed in companies and tradesmen's shops, as well as the self-employed and individual farmers. The number of those employed in companies declined by 3.8 percent on the annual level. The only activities that record employment growth are public administration and defence, as well as social security, 2.8 and 1 percent respectively. The average number of employed in trades and self-employed individuals has increased by 5.9 percent in 1998, while the number of farmers declined by 8 percent. This is a result of non-payment of contributions to the Croatian Pension Insurance Institute from which the State Bureau of Statistics receives data on the number of employed farmers.

Although efforts have been made to improve data on the number of employees, the speed of transition towards a market economy demands permanent changes in statistical samples and higher adaptability of statistics to the increasing number of business subjects and entrepreneurs. Thus there are justifiable doubts that the official number of employees is underestimated, particularly because there is no adequate monitoring of business entities with a small number of employees (up to 10 employees) in the sectors of trade, construction and other service activities which, according to some estimates, are the activities with the largest share in the unofficial economy.

Figure 6: Unemployment



Source: Central Bureau of Statistics

Table 7: Measures of employment and unemployment

	1993	1994	1995	1996	1997	1998
Total employment						
- Central Bureau of Statistics	1,446,606	1,437,059	1,417,427	1,329,547	1,310,918	1,350,147
- Health Insurance Fund	1,573,520	1,564,494	1,588,344	1,599,226	1,604,895	1,430,649
Unemployment						
- Employment Fund	250,779	243,324	240,601	261,022	277,691	287,762
- Health Insurance Fund	166,534	161,660	158,164	174,123	189,844	192,148
Unemployment rate (%)						
- Central Bureau of Statistics	14.8	14.5	14.5	16.4	17.5	17.6
- Health Insurance Fund	9.6	9.4	9.1	9.8	10.6	11.8

Source: Central Bureau of Statistics, Health Insurance Fund, Employment Fund

The Croatian Health Insurance Fund's data on actively insured persons can serve as an alternative measure of employment in Croatia regarding the still relatively high interest of workers in health protection. As shown in Table 8, the alternative rate of unemployment is significantly lower than the official one, but is very close to the unemployment rate obtained using the ILO's methodology.

According to the Labour Survey data from the first half of 1998, made according to the ILO (International Labour Organisation) methodology and internationally comparable, the unemployment rate in Croatia is 11.18 percent. Although significantly lower than the unemployment rate provided by regular research, it records an increase of 1.3 percent compared to June 1997.

Table 8: Unemployment rate - Labour force survey

	Currently Active population	Total employment	Employment in private sector	Employment in public sector and in sector in privatisation	Unemployed persons	Unemployed rate (%)
November 1996	1,710,553	1,540,319	789,319	751,000	170,234	9.95%
June 1997	1,768,167	1,593,008	818,008	775,000	175,159	9.91%
January - June 1998	1,731,916	1,538,372	-	-	193,544	11.18%

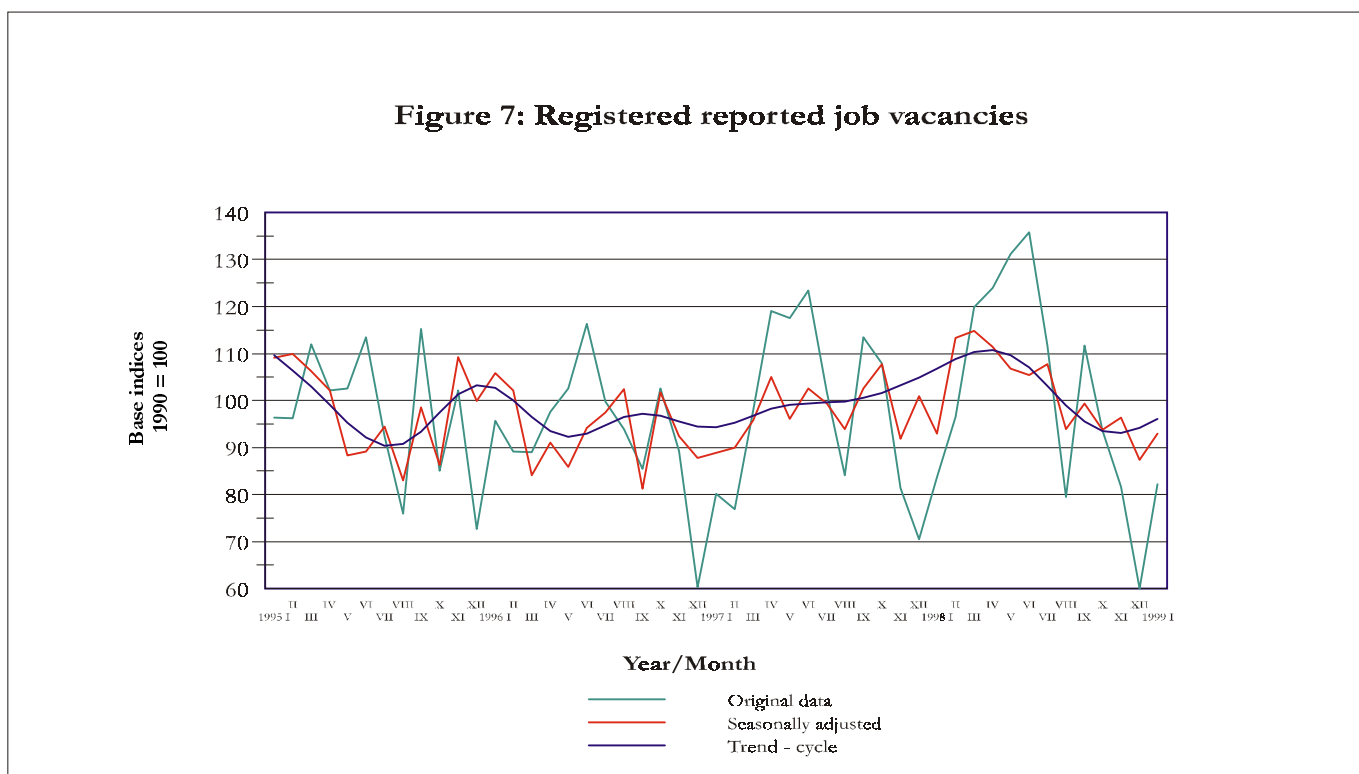
Source: Central Bureau of Statistics

The high rate of registered unemployment and constant decreases in the active population initiated a series of measures by the state directed at the reduction of labour costs, as well as stimulation of employment of new personnel in the second half of last year. These government measures, together with the credit financing of exporters and small and medium-size business through the Croatian Bank for Reconstruction and Development, should increase employment in the subsequent period. This estimate is confirmed by the amount of registered demand for workers, which was 4.6 percent higher in 1998 compared to 1997, and that means an increase of 5,783 new jobs.

Salaries and pensions

The growth of net salaries³ by 16.9 percent nominally or 12.3 percent in real terms in 1997 was supported by an increase in the tax-exempt part of gross wages, and a decrease in the lower limit of the income tax from 25 to 20 percent. In 1998, the Government of the Republic of Croatia undertook a series of measures in order to improve the living standard of employees and to reduce the tax burden on labour. The 2.2 percent contribution for children's allowances was cancelled in July, further increasing net salaries, the 0.8 percent water supply tax on gross salaries was also eliminated, and thus the cost of labour was reduced for employers. During 1998 the Government agreed on a further increase of non-taxable income with trade unions, as well as an increase in the deduction coefficient for dependent family members, the implementation of which commenced on January 1, 1999.

The nominal growth of net salaries in 1998 accounted for 12.8 percent nominally or 6.1 percent in real terms. The average monthly gross salary in 1998 was nominally higher by 12.6 percent. Compared to net salary growth, this indicates a relative reduction of labour costs. The average gross salary in U.S. dollars accounted for US\$ 650 in 1998, which still makes Croatian labour inexpensive and competitive at the international level.



Source: Central Bureau of Statistics

Pensions increased by 16.2 percent nominally (or 11.8 percent in real terms) in 1997 compared to 1996. This is a result of an increase of the tax-exempt share of pensions in 1997, but also of co-ordination with costs of living in January and July. Nominal pension growth in 1998 accounted for 11.4 percent or 5.2 percent in real terms. The share of average paid-in pension contributions in net salaries in 1998 accounted for 49 percent. In addition to payments of pension compensations, by which the state repays its debt to retired persons due to incomplete transfers during the war period, a new Pension Insurance Act entered into force in January 1999. It defines the pension index by growth of salaries and costs of living, and this will additionally influence a change in that relation. To embark upon pension system reform is a priority in the economic policy of the

³ A net salary is defined as the gross salary minus contributions, taxes and surtaxes.

Government of the Republic of Croatia for the year 2000, since the number of retired persons was nearly one million in March 1999, meaning that 1.6 active insured person works for one retired person in comparison with 1990 when the relation was 3.2 to 1.

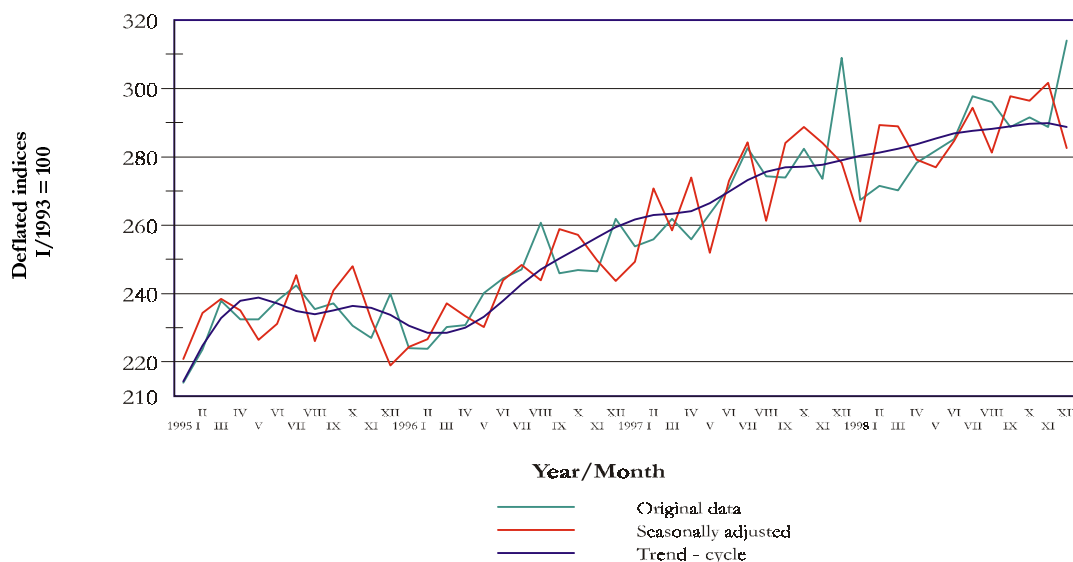
Table 9: Wages and Pensions

(HRK)	1995	1996	1997	1998
Average monthly net wages and salaries	1,818	2,033	2,377	2,681
(nominal growth rate as %)	45.8	11.8	16.9	12.8
Average monthly gross wages and salaries	2,887	3,243	3,668	4,131
(nominal growth rate as %)	34.0	12.3	21.0	12.6
Average monthly pension	922	1,015	1,179	1,314
(nominal growth rate as %)	23.8	10.1	16.2	11.4

Source: Central Bureau of Statistics

The practice of paying the so-called thirteenth salary or "Christmas allowance" commenced at the end of 1997, increasing salary budgets considerably each December. A regulation on non-taxable payment of one-off allowance in the amount of HRK 1,000 was adopted in December 1998. Thus a part of these payments was recorded as a part of the net salary budget in 1998, while until last year it was recorded as an "allowance for executed work to the population and from employment." However, taxes and contributions on salaries indicate the increasing problem of illiquidity in the economy, which means that employers cannot pay out salaries at regular intervals. As of January 1999, the non-taxable income share has increased from HRK 800 to HRK 1,000 per month. The coefficients of personal deductions for dependent family members have been increased progressively, and this considerably increased the net salary of employees supporting several children.

Figure 8: Net wage



Source: Institute of Payments

5. ECONOMIC RELATIONS WITH FOREIGN COUNTRIES

Foreign trade

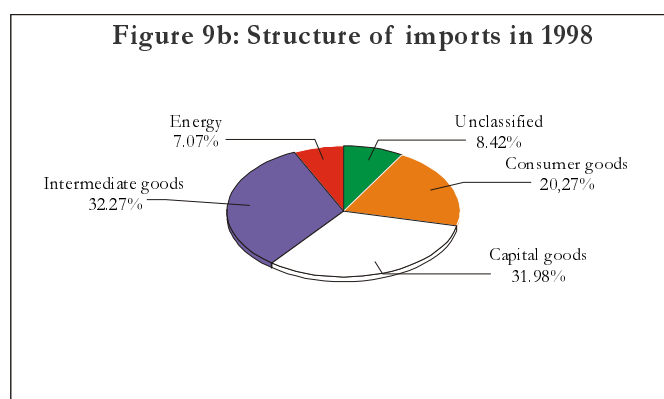
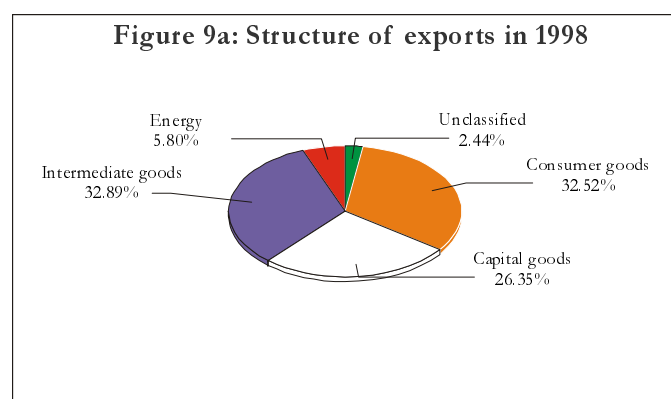
The State Bureau of Statistics published data on foreign trade for all of 1998. The data differ from the Croatian National Bank balance of payments data in terms of volume and classifications. However, the State Bureau of Statistics data are used for foreign trade analysis because they offer more information. The total amount of exports accounted for US\$ 4,541.1 million last year or 8.9 percent more than in 1997. At the same time, commodity exports accounted for US\$ 8,383.1 million or 7.9 percent less than in 1997. It has to be taken into consideration that import value was expressed according to the c.i.f. principle, and the deficit has been overestimated by the amount of insurance and freight services. The adverse balance of the commodity trade accounted for US\$ 3,842 million, and thus it was reduced by 22.1 percent or US\$ 1.1 billion in 1998. The value of f.o.b. commodities exports in HRK was 13.2 percent higher than in 1997, while the value of c.i.f. imports was 4.9 percent less compared to the previous year. The coverage of commodity imports by exports increased from 45.8 percent in 1997 to 54.1 percent in 1998.

Table 10: Merchandise trade 1996 - 1998

(mil. USD)	1996	1997	1998	% change 1997/1996	% change 1998/1997
Exports f.o.b.	4,511.8	4,170.7	4,541.1	-7.6	8.9
Imports c.i.f.	7,787.9	9,104.0	8,383.1	16.9	-7.9
Balance	-3,276.0	-4,933.3	-3,842.0	50.6	-22.1

Source: Central Bureau of Statistics

The highest increase of exports expressed in U.S. dollars was recorded in agricultural and forest products, accounting for 17 percent. Processing industry exports increased by 10.3 percent, and a significant export increase of 348.7 percent was achieved in the shipbuilding industry, 12.9 percent in motor vehicles and trailer production, 5.7 percent in machine and equipment production, 0.8 percent in textile production (which accounts for 11.2 percent of total export volume), and 5.0 percent in radio-television and communications device production. Within the structure of imports expressed in U.S. dollars, the highest decline was recorded in mass consumption products (10.9 percent), while the import of intermediary and capital products declined by approximately 3.5 percent.

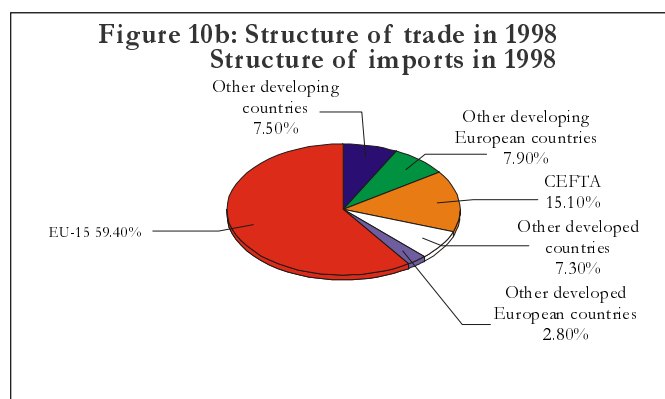
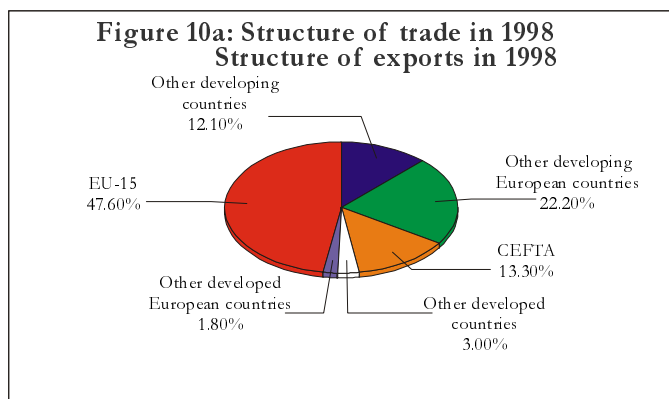


Source: Central Bureau of Statistics

The largest Croatian foreign trade partners are Western European countries with which Croatia traditionally carries out about 60 percent of total imports and about 50 percent of commodity imports. During the last several years, trade with the countries of the former Yugoslavia has been increasing, particularly with Slovenia, Macedonia and the Federation of Bosnia-Herzegovina, with which Croatia signed a Free Trade Agreement. The strategic aim of the Government of the Republic of Croatia for 1999 is accession to the World Trade Organisation. This should accelerate negotiations with CEFTA member states on free trade zones, which are currently under way.

In January 1999, exports expressed in U.S. dollars increased by 10.3 percent and imports decreased by 5.2 percent compared to January 1998. Imports of intermediary products fell by 2.5 percent, and mass

consumption goods imports by 9.9 percent. The decline of monthly trend values of capital and intermediary product imports in the last quarter of last year and at the beginning of this year indicates further slow growth, considering that the imports of these goods represents desired inputs for the faster growth of economic activity. Positive export trends in 1998 should be additionally strengthened by direct stimulative funds from the state budget in the amount of HRK 100 million, which are allocated to Croatian exporters through the Croatian Bank for Reconstruction and Development. Guarantees to exporters in the amount of HRK 700 million will be ensured through the Inter-ministerial Council on Export Credit Financing. All of these measures should improve the competitive position of Croatian exporters, and stimulate the recovery of industrial output.



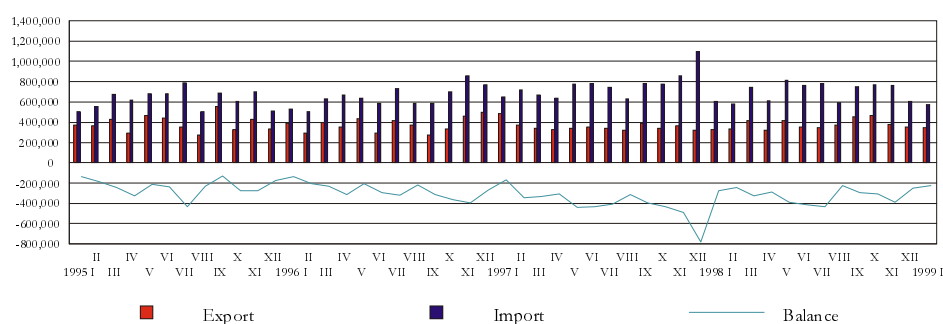
Source: Central Bureau of Statistics

After a high current account deficit of US\$ 2.4 billion (about 12.6 percent of GDP) in 1997, out of which about HRK 500 million are a result of "import fever" in November and December, caused by negative expectations due to the introduction of the value-added tax, a decrease in the current account deficit was recorded in 1998. This is primarily a consequence of the above-described trends in the foreign trade balance. The temporary limitation on the capital account introduced by the Croatian National Bank in April 1998 with the aim of discourage short-term foreign borrowings, used mainly to finance exports, was efficient after all in terms of a reduction in the foreign trade imbalance. The current account deficit in 1998 accounted for 7.2 percent of GDP, and this is 5.4 percent less than in 1997.

Although still preliminary, the data on foreign trade in 1998 have been published. The balance-of-payments current account deficit accounting for US\$ 1,553.8 million was reduced by 36.2 percent in comparison to last year, which is primarily a consequence of deficit reduction in the foreign commodity trade (which dominates on the current account) by 20.2 percent. A surplus on the service account increased by 2.4 percent, while transfers were reduced by 16.9 percent. The negative income account was almost doubled in 1998, which is a consequence of the significant increase in foreign debt interest repayment. A significant increase in net direct foreign investment in the amount of US\$ 763.1 million was particularly significant, as it was three times higher than last year. At the same time, a contraction on the new borrowing item by approximately US\$ 1.37 billion was also noticeable.

In addition to the reduction of the current account deficit in 1998, a significant change in the structure of its financing was also recorded. While 16.6 percent of the deficit was financed by direct foreign and portfolio investments in 1997, in 1998, 45.6 percent of the current account deficit was financed by direct foreign investment. At the same time, the Croatian National Bank's gross international reserves accounted for US\$ 2,815.6 million by the end of December 1998, and in comparison with December 1997 they increased by 10.9 percent or US\$ 276.5 million.

Figure 11: Monthly values of exports and imports in 000 US\$



Source: Central Bureau of Statistics

The total inflow of direct foreign investment accounted for US\$ 2,039.98 million from 1993 to 1998. The largest investors are the United States (41 percent) and Austria (25 percent). The largest investments were made in chemical production (42.9 percent) and the banking system (14.5 percent). The Croatian National Bank conducts surveys continuously on direct foreign investment, which began to grow considerably in 1996 after the Dayton Accords were signed and relations with Paris and London Clubs improved. Direct foreign investment recorded the highest value so far in 1998 between the Asian and Russian crisis. This further confirms the credibility of economic policy, but also a reduction of political risk in the post-war period. A further increase of investments is expected in 1999 primarily because of the already commenced privatisation processes in Croatian Telecommunications and certain rehabilitated banks (Privredna Banka, Riječka Banka and Splitska Banka).

Table 11: Balance of payments 1993 - 1998

(mil. USD)	1993	1994	1995	1996	1997	1998*
Goods, f.o.b.	-960.3	-1,322.5	-3,237.5	-3,651.2	-5,224.4	-4,168.9
Services	1,257.8	1,661.9	1,207.7	1,764.0	2,022.1	2,071.6
Income	-123.8	-76.8	-53.9	1.5	-83.5	-164.5
Current transfers	426.3	523.1	799.9	1,027.8	851.8	708.1
Current account	600.0	785.7	-1,283.8	-857.8	-2,434.0	-1,553.8
Foreign direct investment	77.8	106.3	95.7	513.1	231.2	763.1
Portfolio investment	-0.1	8.6	4.8	27.2	172.7	-54.6
Other investment	225.5	416.1	1,178.0	1,346.7	2,437.5	1,065.1
Capital and financial accounts (without CNB international reserves)	303.2	531.0	1,278.4	1,886.9	2,841.4	1,773.5
CNB international reserves	-449.4	-788.8	-490.2	-418.8	-225.0	-276.5
Net errors and omissions	-453.8	-528.0	495.6	-610.3	-182.4	56.9

* preliminary data

Source: Croatian National Bank

Limited access to the capital market and unfavourable borrowing terms have slowed down the velocity of foreign debt growth. Total foreign debt accounted for US\$ 8,197.1 million by the end of 1998, out of which long-term credit accounted for 94 percent. The total increase of foreign debt since December 1997 accounted for HRK 1.5 billion, which is HRK 320 million less than the debt increase in 1997. With 39 percent of foreign debt as a share of GDP, the Republic of Croatia is still a country with a low debt level, although relative indebtedness in the last two years indicates a significant rising trend. Consideration should also be given to the fact that over 30 percent of debt was inherited from the former Yugoslavia, which was divided among its former republics according to the IMF formula in 1996. Debt servicing to the Paris and London Clubs commenced after this. After the Croatian state was recognised as a credible debtor and after it obtained an investment credit rating by the largest credit agencies in 1997, in addition to reducing borrowing costs for the state sector, a way of financing of the private sector and the public company sector has been created. These sectors have shown a significant increase in debt in the last two years.

Table 12: Debt ratios

(%)	1994	1995	1996*	1997	1998
External debt/GDP	19.34	17.74	24.36	34.48	39.03
Exports of goods and services/External debt	253.70	217.37	166.87	123.09	104.49
Debt service/GDP	2.26	2.42	2.08	3.22	3.47

*data for 1996 to 1998 include Paris and London club debt

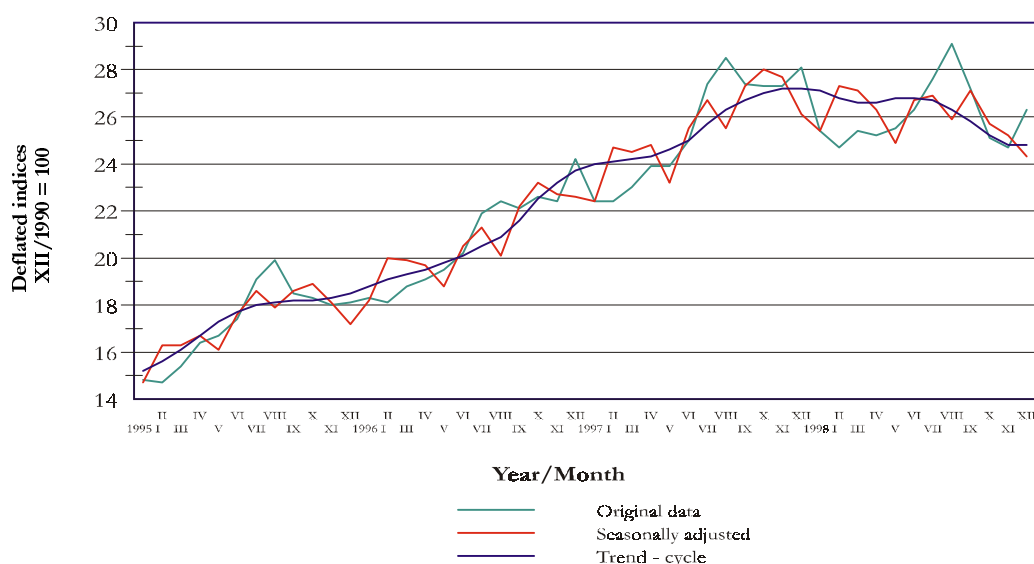
Source: Croatian National Bank

6. MONETARY TRENDS

The main objective of monetary policy since the introduction of the Stabilisation Program has been the maintenance of price and exchange rate stability. Credit expansion commenced in 1997 and resulted in the explosion of the balance-of-payments current account deficit, so that it was necessary to undertake corresponding corrective measures. Thus the central bank prescribed obligatory foreign exchange reserves for short-term foreign borrowing with the aim of discourage borrowing for consumer goods imports. The measures introduced to discourage foreign borrowing reduced credit aggregates in the domestic market. The growth rate of credit volume declined from 44 percent in 1997 to 23 percent in 1998, out of which the consumer credits were increased by 45 percent in comparison with 1997 when the rate was 93 percent. The credit growth rate for companies was also halved.

The money supply was reduced by 1 percent in 1998 compared to 1997, when it increased by 21 percent. The cyclical trend indicates a decrease in the money supply in real terms by 8.8 percent last year. A decrease in the money supply together with high demand caused an increase in the price of money - interest rates, which were at a rather high level in real terms up to then. Together with the reallocating effects of the introduction of the VAT, company deposits decreased by 15.8 percent last year, confirming the fact that company liquidity has been significantly worsened. At the same time, secondary sources of liquidity have been reinforced. Namely, during 1998 the use of bills issued by the Republic of Croatia and treasury bills issued by the Finance Ministry was allowed as collateral for lombard loans at the same percentage at which treasury bills issued by the Croatian National Bank can be used.

Figure 12: Real money supply M1

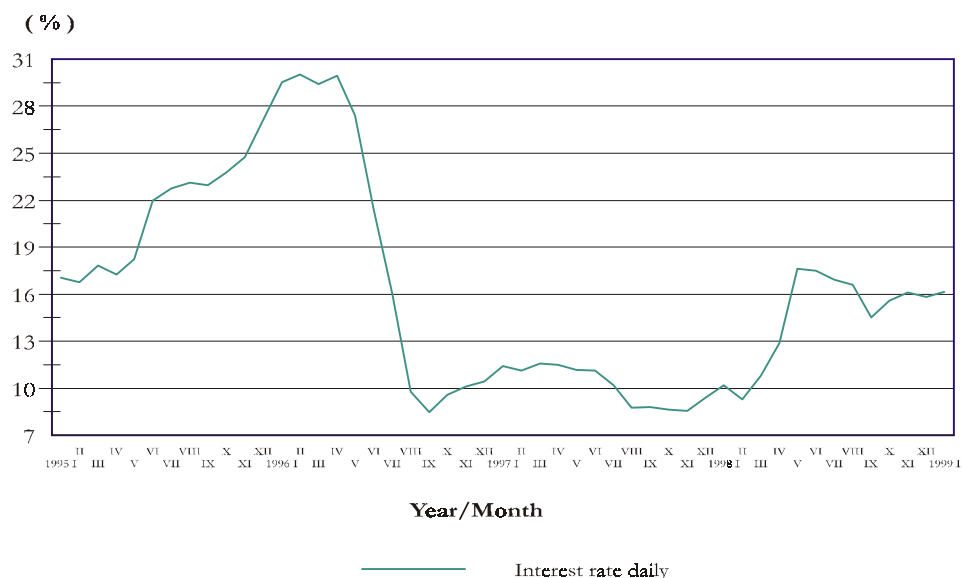


Source: Croatian National Bank

Foreign currency deposit growth in 1998 accounted for 20 percent in comparison with 42 percent growth in 1997. The amount of foreign currency deposits accounted for HRK 37 billion by the end of 1998. In contrast, time-deposit domestic currency savings stagnated. The resort to foreign currency savings is the

consequence of negative expectations this year. Therefore, the primary objective of the Croatian Government is to further insist on stable trends in prices and the exchange rate.

Figure 13: Interest rate on the money market - daily



Source: Croatian National Bank

Net claims on Central Government in monetary survey were almost stagnant if December 1998 is compared with the same period in 1997. Namely, after a significant reduction of the government's net debts in 1997 from HRK 14.63 billion to HRK 7.33 billion, this item decreased by only HRK 200 million. Although the government settles its obligations to commercial banks duly and on time, a consolidation of the banking system, which commenced in April 1998 with Dubrovačka Banka, increased the public internal debt by HRK 500 million in the item related to bonds for the rehabilitation of the banking system. Kuna depreciation in the second half of this year also increased the public internal debts, since 90 percent of public internal debt was indexed according to DEM trends.

Table 13: Monetary and credit aggregates

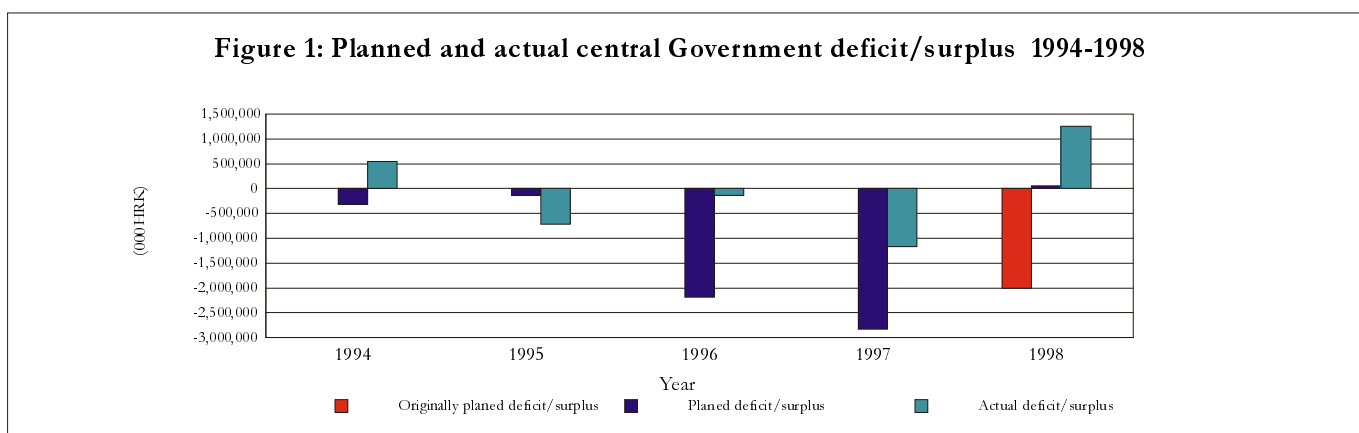
(millions of kuna, end of period)	1996	1997	% change 1997/1996	1998	% change 1998/1997
Reserve money	8,770.4	10,346.1	18.0%	9,954.2	-3.8%
Money M1	11,409.4	13,795.2	20.9%	13,595.0	-1.5%
Broadest money M4	36,595.6	50,342.7	37.6%	56,558.7	12.3%
Domestic credit	24,885.7	33,488.3	34.6%	43,899.0	31.1%
Net domestic assets	33,488.6	48,264.2	44.1%	58,959.7	22.2%

Source: Croatian National Bank

II. CENTRAL GOVERNMENT BUDGET IN 1998

The most important characteristics of 1998 fiscal policy were the introduction of the value-added tax, the commencement of the gradual cost reduction of labour and the global financial crisis. These three factors conditioned a revision of the 1998 budget, which was drawn up in July 1998. However, the global financial crisis and the closing of the international capital market to transition countries, in particular after the Russian crisis, determined the restrictive nature of 1998 fiscal policy - in terms of the central budget surplus. The central budget surplus on a cash basis amounted to HRK 1,256.7 million, while the consolidated central government surplus amounted to HRK 882.1 million. However, bonds in the amount of HRK 1,047 million were issued for the central budget's outstanding liabilities in December 1998, which reduced the actualised central budget surplus in real terms.

The position of 1998 fiscal policy certainly contributed to the necessary reduction of the balance of payments deficit. However, it had a pro-cyclical effect, particularly in the second half of the year. Under the circumstances of a slowdown in economic growth, the central budget surplus, enhanced by domestic and foreign financial restrictions, contributed to the stagnation of economy. Another particularly strong reason for this stagnation was foreign debt repayment in the second half of the year. In terms of actualised central budget deficit or surplus, fiscal policy has, in the past five years, managed to exceed planned results, as shown in Figure 1. Namely, in all years, with the exception of 1995, the year in which the military operations "Flash" and "Storm" to liberate the occupied parts of the country were staged, the actualised central budget deficit was lower than planned. In this respect, 1988 is very indicative, in particular for two adjustments - the first was budget revision aimed at its balancing, while the second adjustment took place in the second half of the year, when the surplus necessary for regular debt repayment was accumulated.



Thus fiscal policy displayed the necessary flexibility in its adaptation to the economic climate. However, this flexibility was, as a rule, necessary to earn revenues higher than those forecasted for the budgets in the years under review, so that public expenditure continually grew. As a result of this process, Croatia's public sector is one of the strongest in Europe, as compared with other countries. Moreover, while other countries have a trend of decrease in the size of the public sector - which occurred as a result of the requirement to meet the criteria set for developed countries by the Maastricht Treaty and the transition processes in the former socialist bloc - the public sector in Croatia has been growing continually. This conclusion is not subject to the dilemmas on the actual and possible excessive estimates of the official GDP size. As explained in detail in the chapters on trends in the central government and central budget, the major generators of public sector growth are extra-budgetary funds and, to a lesser extent, local administration and self-government. In addition to the continual generation of the need for growth in transfers from the central budget, extra-budgetary funds also continually generate pressure to increase the public sector deficit. In this manner, extra-budgetary funds appear as the major source of problems, whose resolution will require adequate adjustments in 1999 but also in the future years.

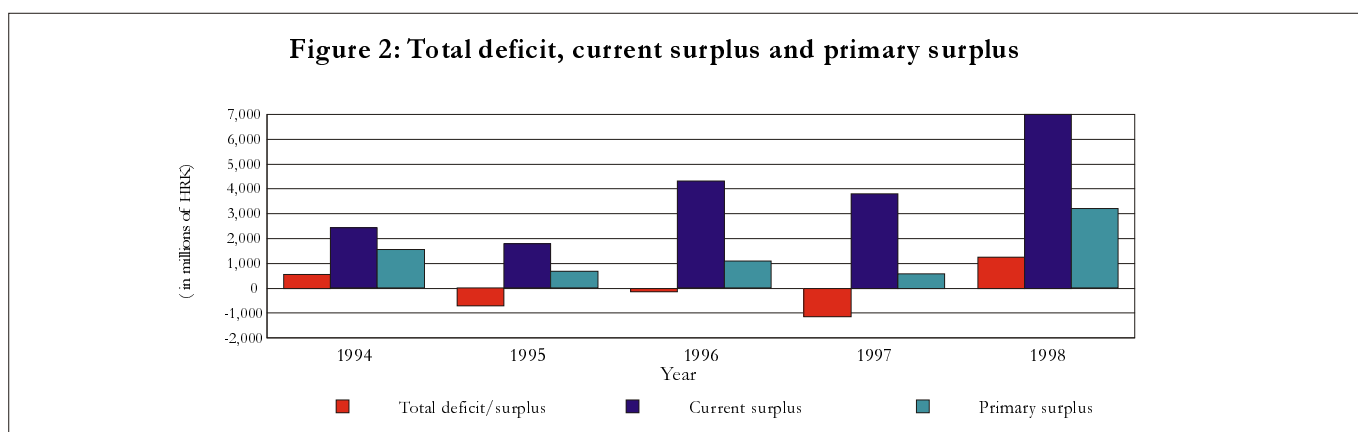
The growth trend of extra-budgetary funds, primarily pension and health insurance funds, and the consequent increasing need for transfers from the central budget, continued in 1998. In addition to a slowdown in economic activity, a lack of fiscal discipline in the collection of contributions and the inefficient system of organising extra-budgetary funds resulted in lower revenue growth than planned, while increases in expenditures of both funds was much more rapid than increases in their revenues. Revenues from

contributions to the former Pension and Disability Insurance Funds (now the Croatian Pension Insurance Institute) in the period between 1994 and 1998 increased 46.23 percent, while in the same period pension costs increased 145.8 percent. Consequently, transfers from the central budget to the pension fund increased from HRK 285.2 million in 1995 to HRK 3,559.5 million in 1998. However, in addition to these transfers, the Pension and Disability Insurance Fund was financed by banks, while the Croatian Health Insurance Institute generated a significant amount of outstanding liabilities.

In spite of a lack of funds, obligatory contributions for the financing of extra-budgetary funds are high, which results in a high unit cost of labour. Despite the abolishment of contributions for children's allowances and water contributions, the burden on labour by way of contributions was only slightly reduced, from 43.4 percent to 40.4 percent, which means that the unit cost of labour remains high, with all of the accompanying negative consequences for the competitiveness of the Croatian economy. Therefore an increase in the efficiency of extra-budgetary funds in terms of revenue collection, as well as the restructuring of the system of their financing, have been imposed as the primary objectives of 1999 fiscal policy and in the future medium-term period, because this is the only way to ensure a necessary decrease in public expenditure and the overall tax burden.

The current surplus in 1998 was HRK 7,136.4 million, which is the largest amount of state savings in the past four years, as presented in Figure 2.

Also, a primary surplus has been recorded for four consecutive years, which means that total revenues are larger than non-interest expenditures and shows that interest is paid from revenues and not from debts.



1. REVISION OF THE 1998 BUDGET

In December 1997, the 1998 budget was adopted, which provided for a central government budget deficit of HRK 2,010 million, that is total revenues of HRK 39,135 million as well expenditures in the amount of HRK 37,477. However, in July 1998 the budget was revised. The most important changes in budget revenues and expenditures provided by budget revision are presented in Table 1.

Table 1. Changes in central budget's revenue and expenditure due to the revision of the budget

(000 HRK)	Budget 1998	Revised Budget 1998	Index Rev. Budget/Budget
Total revenue and grants	37,123,996	44,596,194	120.13
Total revenue	37,123,996	44,596,194	120.13
Current revenue	34,954,810	42,277,008	120.95
Tax revenue	32,795,663	40,039,486	122.09
Non tax revenue	2,159,147	2,237,522	103.63
Capital revenue	2,169,186	2,319,186	106.92
Grants	0	0	
Total expenditure and lending minus repayments	39,134,564	44,596,194	113.96
Current expenditure	31,988,195	35,650,979	111.65
Expenditures on goods and services	21,700,193	22,803,087	105.08
Interest payments	2,572,250	2,505,889	97.42
Subsidies	2,380,324	3,059,593	128.54
Transfers	5,335,428	7,282,410	136.49
Capital expenditures	5,489,182	7,283,828	132.69
Lending minus repayments	1,657,187	1,661,387	100.25

The major reasons for the budget revision were:

- the abolishment of contributions for children's allowances (2.2 percent of gross wages) and water contributions (0.76 percent of gross wages) as of 1 July 1998. The mentioned contributions were abolished in order to implement a policy of employment incentives determined by the Government Program of Measures for the Implementation of the National Employment Policy,
- a balancing of the central budget which took place because government bonds denominated in Japanese yen could not be issued, as originally planned, due to the Asian crisis,
- much higher revenues from the value-added tax in relation to the amount foreseen in the 1998 budget.

In addition to the aforementioned, the growth of revenues opened room for a certain increase in central budget expenditures. In relation to the original budget, total revenues in the revised budget grew 20.13 percent, while total expenses increased 13.96 percent. In relation to the actual 1997 budget, an increase in total revenues by 31.8 percent and an increase in total expenses by 27.39 percent were planned in the revised budget. However, changes in the central budget related to the manner of financing of children's allowances and the Croatian water management administration (Hrvatska vodoprivreda) make it impossible to directly compare central budgetary expenditures determined by the revised budget and budgetary expenditures in previous years. Namely, expenses incurred in the central budget for these purposes are not a new type of expense but expenses which were previously charged to the appropriate extra-budgetary units, so that the real amount of increased expenses is reflected in the central government's consolidated balance sheet. Considering the change in financing children's allowances and the Croatian water management administration, the central budgetary expenses increased by 7.64 percent in the revised central budget.

VAT revenues were funds that made a major contribution to the growth of revenues planned for the year. VAT revenues increased 33.7 percent in the revised budget, while income tax revenues grew by 6.4 percent. Also, sales tax revenues of HRK 1,890 million were planned by the revised budget as a separate item. Namely, in the original 1998 budget, sales tax revenues were presented together with the estimate of value-added tax revenues, as significant revenues were not expected from the sales tax. However, the volume of retail sales in late December, as a result of intensified purchasing during the Christmas period and due to fears of a possible increase in prices after the introduction of the value-added tax, as well as sales tax payments for old debts, generated sales tax revenues of HRK 1,686 million already by June 1998. For this reason, sales tax revenues were stated as a separate item in the revised budget.

The major increase in expenses planned in the revised budget related to current transfers - HRK 1,946.9 million, that is 36.49 percent, which is a result of the growth of transfers to the Pension Fund and the aforementioned abolishment of the two contributions. Transfers to the Pension Fund increased from the previously planned HRK 2,370.4 million to HRK 3,271.9 million in the revised budget, that is by 38.03 percent. This increase is a result of the growth of transfers to disability pensions and pensions for the families of Croatian war veterans of HRK 300 million and HRK 100 million for pensions subsidised due to an insufficient amount planned for these purposes in the original budget. The transfer also includes an additional HRK 500 million intended for the reconciliation of pensions for the period between 1990 to 1998, pursuant to the Pension Adjustment Act, the so-called "Minor Pension Act". Due to the aforementioned discontinuation of contributions for children's allowances, HRK 600 million was planned in the revised budget for transfers to the State Institute for the Protection of the Family, Maternity and Youth and, due to the abolishment of water contributions, HRK 135 million for the Croatian water management administration. This increase was also reflected in transfers to the Employment Fund; an additional HRK 30 million was planned in the revised budget for the employment of trainees, in accordance with the Employment Incentive Measures of the Government of the Republic of Croatia.

Apart from current transfers, the revised budget estimated significant growth in subsidies in an amount of 28.54 percent. The major cause for this growth was the increase of subsidies for the Croatian national railway company by 24.64 percent, or HRK 310 million, and for agriculture by 27.37 percent, or HRK 176 million. At the same time, the revised budget also provided for an additional HRK 70 million intended for the Agricultural Development Fund, which is reflected in the increase in net borrowing. A new type of subsidies which was introduced in the revised budget are subsidies for tourism, intended for hotels and tourist complexes, in the amount of HRK 194 million. The purpose of this subsidy was to alleviate the effects of the introduction of the value-added tax on the tourism sector. Namely, accommodation services for foreign tourists were exempted from value-added tax payments, while accommodation services for domestic tourists were subject to a 10 percent sales tax.

Expenses for goods and services, as estimated in the revised budget, grew 5.08 percent, which was primarily the result of an increase in expenses arising from salaries in an amount of HRK 600 million and an increase in expenses for the care of refugees and displaced persons in an amount of HRK 200 million. The growth of expenses for salaries was a result of an agreement between the Government and labour unions on the disbursement of the Christmas allowance, children allowances and anniversary bonuses for civil servants.

Capital expenditures increased in the revised budget by 32.69 percent, i.e. by HRK 1,794.6 million. This increase occurred mostly as a consequence of the growth of expenses for the construction and maintenance of roads, for which an additional HRK 453 million was planned in the revised budget, of which HRK 352 million went to road construction. Thus the total funds intended for the construction and maintenance of roads increased to HRK 1,602.9 million.

Capital transfers grew by HRK 998 million, of which HRK 593 million were transfers to the Croatian Health Insurance Institute (HZZO) to cover liabilities to suppliers, HRK 150 million to reconstruction and HRK 150 million for the equity share of the Croatian Bank for Reconstruction and Development. The transfer to the Croatian Health Insurance Institute to cover liabilities to suppliers was offset by the transfer of shares from the HZZO's portfolio to the portfolio of the Croatian Privatisation Fund. Thus the total subsidies for the HZZO planned in the central budget grew from HRK 852 million to HRK 1,513.5 million, which actually covered the increased costs of the HZZO which were a result of the introduction of the VAT. Namely, under the previous sales tax system medicine was subject to a 5 percent tax rate.

The revised budget was a balanced budget, which provided for current savings of HRK 6,626.1 million. This ensured the coverage of capital expenditure by way of budgetary current savings at the amount of 93.17 percent.

2. EFFECTS OF THE INTRODUCTION OF THE VALUE-ADDED TAX

Since the beginning of 1998, the value-added tax in the consumption form has been applied in Croatia instead of the sales tax on goods and services. Consumption form means that final domestic consumption constitutes the value-added tax base, while the calculation is done according to the credit method, which means that the net tax base is determined as the difference between the amount of the VAT stated on sales invoices and the amount of the VAT stated on purchase invoices. This method of calculation is characterised by simplicity and an integrated control mechanism. Namely, the right to a deduction of the pre-tax amount is possible only for regularly invoiced purchases, which means that the manner of functioning of the value-added tax limits the space and motives for tax evasion. It is exactly the integrated mechanism of self-control which contributed to firmer fiscal discipline and a reduction of the "grey economy," which was one of the main reasons for its introduction.

The value-added tax is calculated at a 22 percent rate for all goods and services delivered and rendered in Croatia. Tax relief without the right of pre-tax claims are applied to the lease of flats, banking and savings institution services, insurance companies, medical and dental services as well as the services and goods provided and rendered in social care and educational and cultural institutions. Only exported goods are exempt from the VAT with the right to a pre-tax deduction (zero rate).

The value-added tax payers are all businesses and self-employed individuals which, in 1997, delivered and rendered goods and services in a value exceeding HRK 50,000. Businesses and self-employed individuals whose income was lower than HRK 50,000 could voluntarily register in the VAT system. At the beginning of 1999, the threshold for mandatory registration in the system was raised to HRK 85,000.

There were three accounting periods in 1998. Small companies and individuals - VAT payers - whose quarterly income did not exceed HRK 50,000 calculated and paid the VAT quarterly. Utilities and public companies that normally issue invoices monthly calculated and paid the VAT monthly, while all other taxpayers paid the VAT every two weeks. As of the beginning of 1999, the accounting period has been extended to one month. This change relates to all businesses except small companies and individuals subject to the VAT payment; they are obliged to calculate and pay the VAT quarterly.

The value-added tax system, as applicable from 1 January 1998, was determined by the law promulgated by the Croatian National Parliament in July 1995. Pursuant to this law, the VAT should have been introduced on 1 January 1997, which was postponed in order to ensure more comprehensive and better preparation of taxpayers and the public as well as the tax administration. Despite a sufficient period of preparation, the behaviour of economic entities in the months immediately preceding the introduction of the value-added tax was to a large extent determined by the uncertainty concerning the effect which the value-added tax would have on their business and the overall macroeconomic conditions, primarily prices. The most obvious indicator of this uncertainty is the significant growth of imports in November and December 1997. According to estimates, in November and December 1997 the one-time effect of the introduction of the VAT on the growth of imports and, consequently, on the increase in the balance of payments deficit, amounted to between US\$ 500 million and US\$ 700 million, or between 2.5 and 3.5 percent of GDP. In this manner, the introduction of the VAT significantly contributed to the balance of payments deficit of 12.5 percent of GDP in 1997. Also, the acceleration of invoicing delivered goods and services was perceived, while a negative atmosphere was created in the public in relation to the possible effect of the VAT on price trends.

2.1. THE EFFECT OF THE INTRODUCTION OF THE VAT ON PRICES AND THE ACTIVITIES OF THE CONSUMER SUPPORT COMMISSION

In order to provide the public with more information and to prevent producers and retailers from using the VAT as an excuse for raising prices, the Government established the Consumer Support Commission. Although the standard sales tax rate was higher than the VAT rate and despite a significant cumulative effect in the sales tax system, there was a real danger of producers and retailers justifying any price hikes by citing the VAT. Namely, the value-added tax was expected to cause an increase in the prices of certain goods and

services. This, in the first place, related to foodstuffs and services which were subject to a lower tax rate (15.5 percent for foodstuffs, some basic provisions being exempted from taxation), while services were taxed at a 10 percent rate. However, due to the cumulative effect, the increase of prices caused by the introduction of the VAT should have been much slighter than the mathematical difference in tax rate percentages. On the other hand, the VAT was introduced at the beginning of the year, at a time when prices are adjusted in order to achieve the business objectives set for the subsequent year. Therefore, the Commission's duty was to prevent the justification of any change in prices, including those that would occur even without the introduction of the VAT, through tax reform.

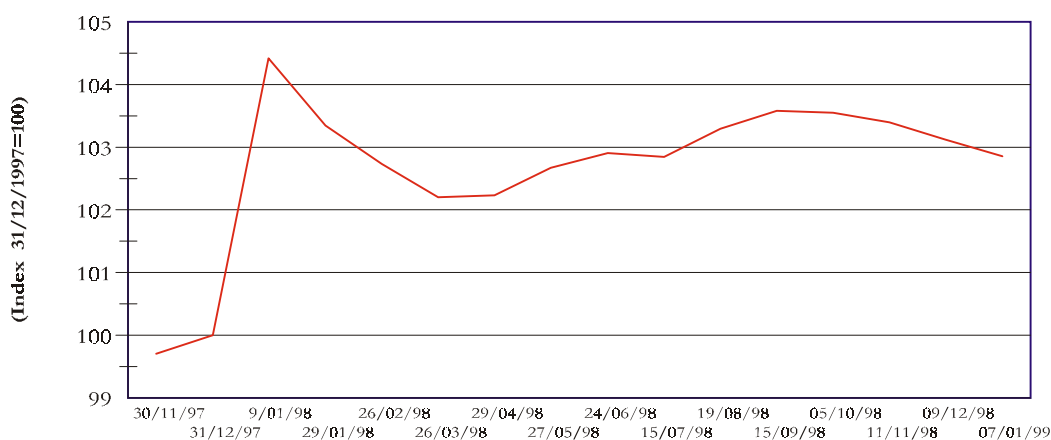
The task of the Commission was to inform consumers of any excessive increases or insufficient reductions in the prices of certain goods and services justified by the introduction of the value-added tax. The Commission did not have any executive authority, but it was obliged to inform consumers, through the media, of changes in prices that could be justified by the value-added tax and of the real trends in prices at the most frequented outlets.

Pursuant to these tasks, the Commission organised a survey of the prices of over 60 goods and services in 21 cities. The recorded prices served as the basis for the calculation of the Commission's price index as an aggregate indicator of price trends on the level of cities and the entire country. The Commission submitted 15 notices to consumers in the highest-circulation daily newspapers about changes in the prices of specific products sold in specific outlets. In addition, a separate telephone and fax were opened for comments, suggestions and observations of consumers in the period from 10 January to the end of May 1998.

The Commission regularly informed the Government of the Republic of Croatia of its activities. The basic conclusions of the Commission on price trends after the introduction of the VAT are set below:

- After the introduction of the VAT, the price levels remained within expected parameters. A 2.4 percent one-time average growth in prices in January was offset by their subsequent decrease in February, March and April, after which period prices continued to change according to their usual dynamics. Price trends determined by the Commission's index are shown in Figure 3.
- The perceived average decrease in prices in February, March and April should have been even more pronounced. The Commission's argument in favour of this conclusion were producer price trends, according to the State Bureau of Statistics, and the trends in prices of the goods included in the consumer goods basket as determined by the Commission. In the first four months of 1998, producer prices dropped 1.5 percent in relation to December 1997, partly as a result of the disappearance of any cumulative effect. Moreover, the fall of producer prices continued throughout 1998, so their total decrease in 1998 was 1.2 percent. To the contrary, retail prices grew 5.4 percent, of which 2.4 percent is considered the result of the introduction of the VAT. It is exactly this difference in the producer and retail price trends, which indicates that the introduction of the VAT was partly used for an increase in profit margins. Also, the Commission's consumer goods basket of only 64 products and services contains some products which raised in price after the introduction of the VAT by a percentage higher than the one which can be considered a result of the change of tax rates. Moreover, even within such a small sample it was possible to find examples of products which became subject to a lower tax rate after the introduction of the value-added tax and whose price have not decreased, not even as much as the tax rate difference.
- Despite the attention of the media directed at trends in food prices after the introduction of the value-added tax and despite concerns over the effects of the possible growth of food prices on citizens' living standards, the data issued by the Commission show that the greatest pressure on citizens' living standards after the introduction of the VAT occurred in the form of an increase in utilities costs. This conclusion is clearly illustrated in Figure 4, which represents trends in the Commission's index, by product group. Thus utility costs increased on average by 31.4 percent in Bjelovar, 27.4 percent in Sisak and 25.4 percent in Dubrovnik, while Koprivnica and Požega suffered the least; the average increase in utilities service costs in these two towns was 1.9 percent and 3.2 percent respectively.

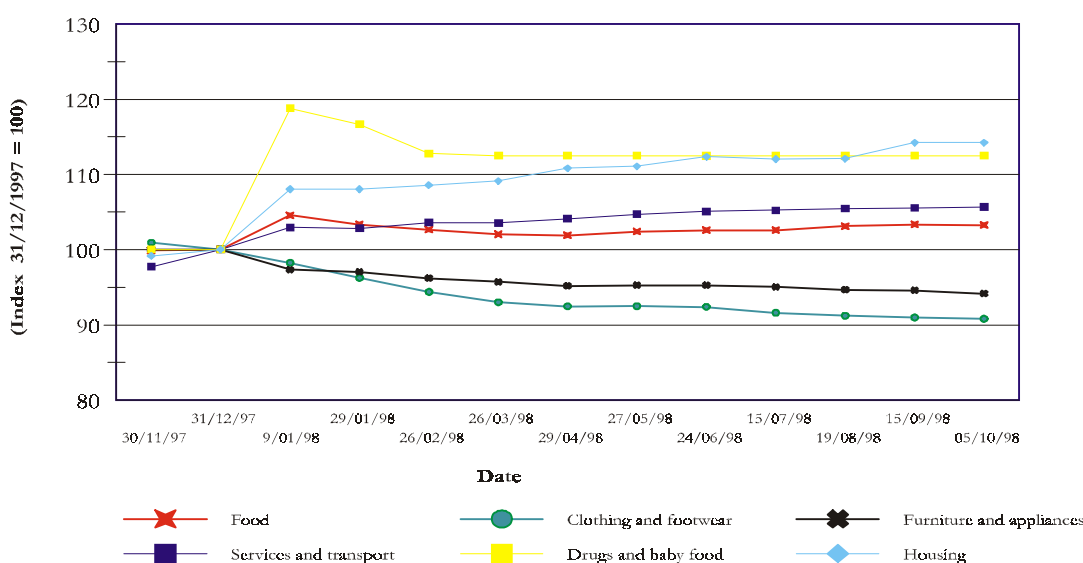
Figure 3: Prices after the implementation of VAT according to Consumer Support Commission data



The best proof of the burden which the increase in utility costs imposed on household budgets are the complaints of users on trends in utilities costs and the costs of services provided by public companies, received mostly through telephone and fax messages from consumers. The Commission concluded that the principal reason for such trends in utility services costs was the monopoly of their suppliers and recommended that the Government of the Republic of Croatia take measures to curb the uncontrolled growth of the aforementioned prices and measures which would contribute to improved control over the operation of these companies.

- The continual growth in personal service prices as well as utilities costs definitely confirm the basic fact that taxes are not the only or decisive price determinant. The prices of any product change even without tax rate changes, and are the result of business policy as well as of the market environment in which economic entities operate. Therefore, the elimination of monopolistic market structures, an increase in the competition level and the greater openness of economy have a positive effect on consumer.
- In the past period, Velika Gorica and Sisak were towns in which the highest price increases were recorded, 9.79 percent and 7.19 percent respectively. As to general price levels, Zagreb is by far the most expensive city in Croatia, and Karlovac, Pula and Velika Gorica follow. At the same time, the lowest increase in the past ten months was recorded in Virovitica and Slavonski Brod, while Koprivnica and Požega were the least expensive towns. According to the available data, the average price growth after the introduction of the value-added tax was less pronounced than in the towns located near the country's border. It can also be concluded that the level of prices was lower in the towns located near the country's borders.

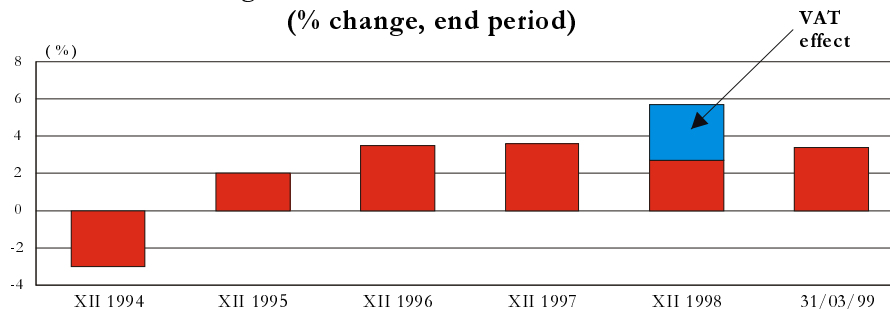
Figure 4: Consumer price index by groups of products and services - according to Consumer Support Commission data -



At the end of 1998, the data released by the State Bureau of Statistics showed that retail prices in December 1998 exceeded those of December 1997 by 5.4 percent. According to the State Bureau of Statistics, at the same time retail prices rose 2.4 percent in January 1998 in relation to December 1997, which indicates that the one-time effect of the introduction of the VAT on prices was approximately 2.4 percent. Figure 5 clearly shows that, excluding the one-time effect of the VAT in 1998, inflation trends in 1998 fully fit into the trend established after the stabilisation program. This is also confirmed by the trends in the retail price index in the first three months of 1999, which indicates a 3.4 percent growth of prices in relation to the same period last year.

It can be concluded that the introduction of the VAT was successful with regard to its effect on price trends.

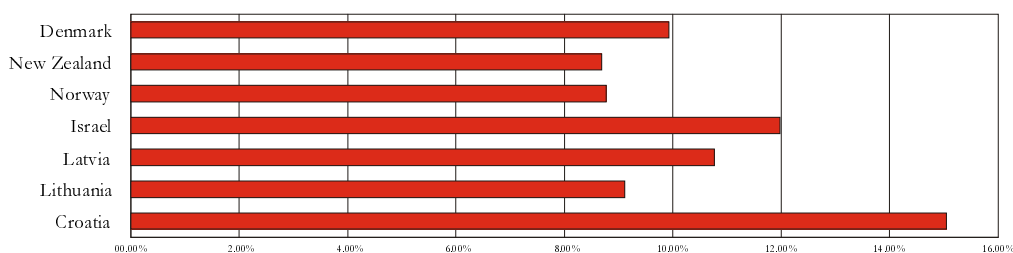
Figure 5: Consumer Price Inflation (% change, end period)



2.2. VAT REVENUES AND THE GROSS DOMESTIC PRODUCT LEVEL

The fiscal effects achieved by the introduction of the VAT certainly exceeded expectations. Revenue trends from the newly-introduced tax in the first half of the year showed that the amount of the paid VAT by the end of the year would significantly exceed revenues planned in the original 1998 budget. Therefore the VAT, as already noted, is an item which made a major contribution to the revised budget for 1998. VAT revenues increased in the revised budget from HRK 15,039 million to HRK 20,102 million, which means a 67.8 percent growth in revenues. The realisation of the 1998 budget shows that an amount exceeding the one planned by the revised budget was collected by means of the VAT.

Figure 6: VAT as % of GDP among single rate VAT countries



It was precisely the high revenues generated by the VAT in the amount of HRK 20,228 million, which provoked the suspicion in the Ministry of Finance that the official statistics significantly underestimated the Croatian gross domestic product. Namely, starting with the data issued by the State Bureau of Statistics on the level of GDP in 1997 and the expected 1998 growth rate, we arrive at a GDP amount of approximately HRK 135 billion in 1998. As a result, VAT revenues account for approximately 17 percent of GDP, which would make Croatia the most successful country in the world when it comes to the collection of VAT revenues. There is no other country in the world with a single VAT rate that realises such high revenues. This, as illustrated by Figure 6, also includes Denmark, where the VAT rate is 25 percent. As in Croatia, there are very few items exempted from tax payment. On the other hand, Israel generates 11.97 percent of its GDP by means of the VAT, but banking services are taxable as well.

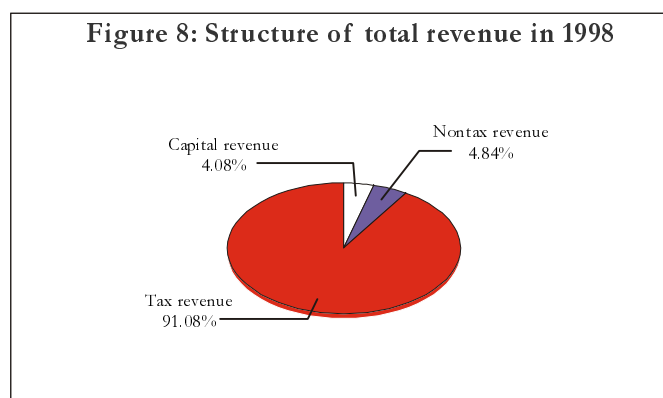
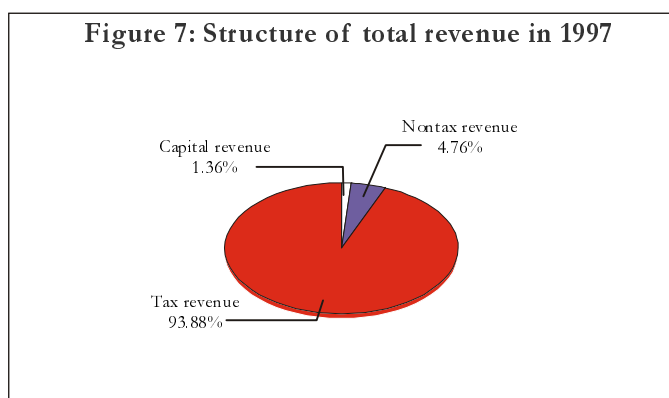
Pursuant to these arguments, a regression analysis was made on the basis of panel data for a sampling of countries that apply a single VAT rate. The analysis showed that one percentage point of the value-added tax produces 0.4 percent of GDP generated by VAT revenues, which means that the VAT with a 22 percent rate should create about 9 percent of GDP. Considering the specific characteristics of the economic structure in the Republic of Croatia - in relation to the analysed countries - such as large citizens' transfers from abroad, a 90 percent share of personal and government expenditures in GDP, the importance of export services (tourism) without the right to a deduction of pre-tax amounts, etc., it was concluded that the share of the VAT in GDP cannot exceed 11.5 percent of total GDP. On this basis it was calculated that the size of GDP arising from the described revenues in 1998 should be about HRK 179 billion. The size of GDP in the previous years was calculated on the basis of GDP growth rates in the respective years, as calculated by the State Bureau of Statistics.

The illiquidity problem, which escalated in 1998, is associated by many with the introduction of the value-added tax. By increasing the level of fiscal discipline, the value-added tax has contributed to an intensification of this problem, but the value-added tax itself is not the cause of the illiquidity problem. The illiquidity problem is older than the VAT, which is clearly indicated by as much as 71 percent of the total recorded uncollected receivables older than one year. Moreover, retail and wholesale trade are on top of the list of industries with the highest number of economic entities with blocked transfer accounts. On the other hand, it is precisely these two industries, in particular retail trade, which should "roll in money", which is an additional proof that the causes of their illiquidity lay beyond the VAT.

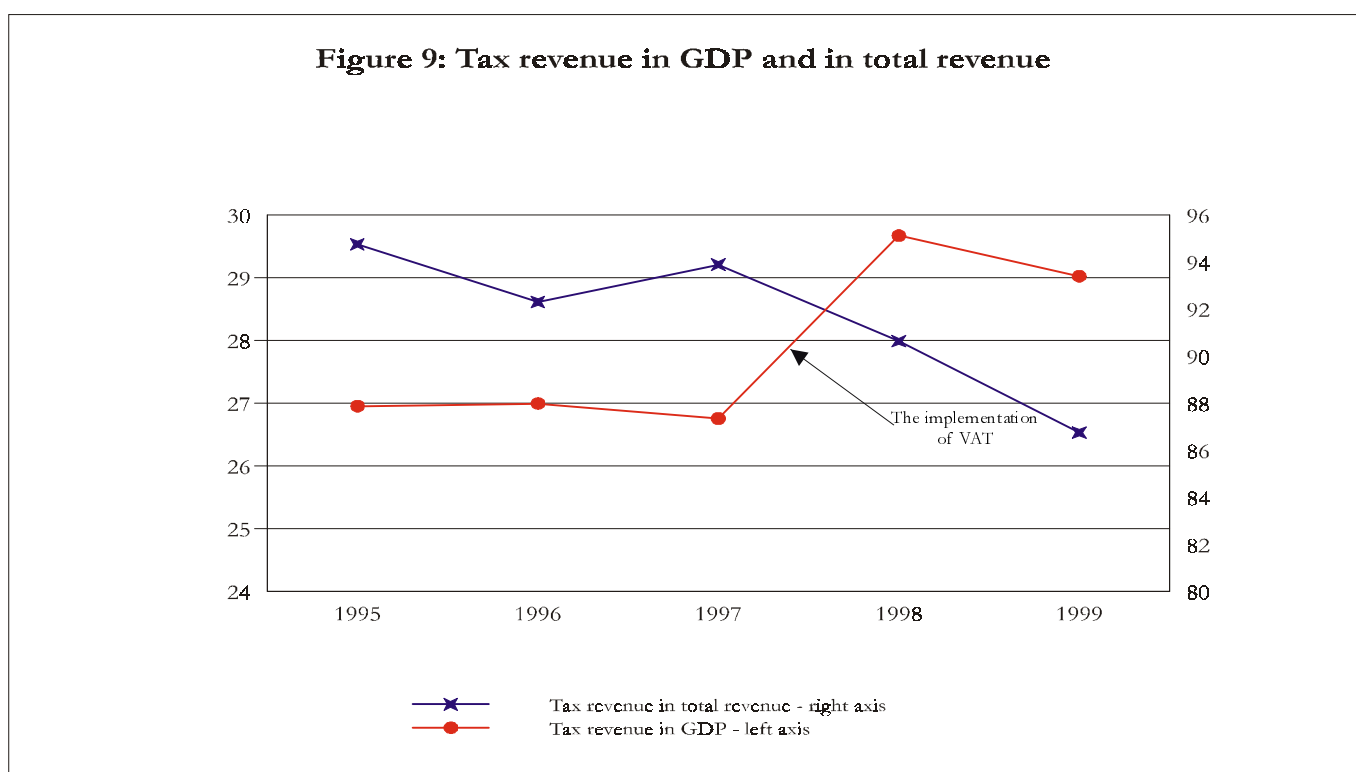
3. 1998 CENTRAL BUDGET REVENUES OUTTURN

3.1. TAX REVENUE

Changes in the structure of total revenues during the course of 1998 are evident if Figures 7 and 8 are compared.

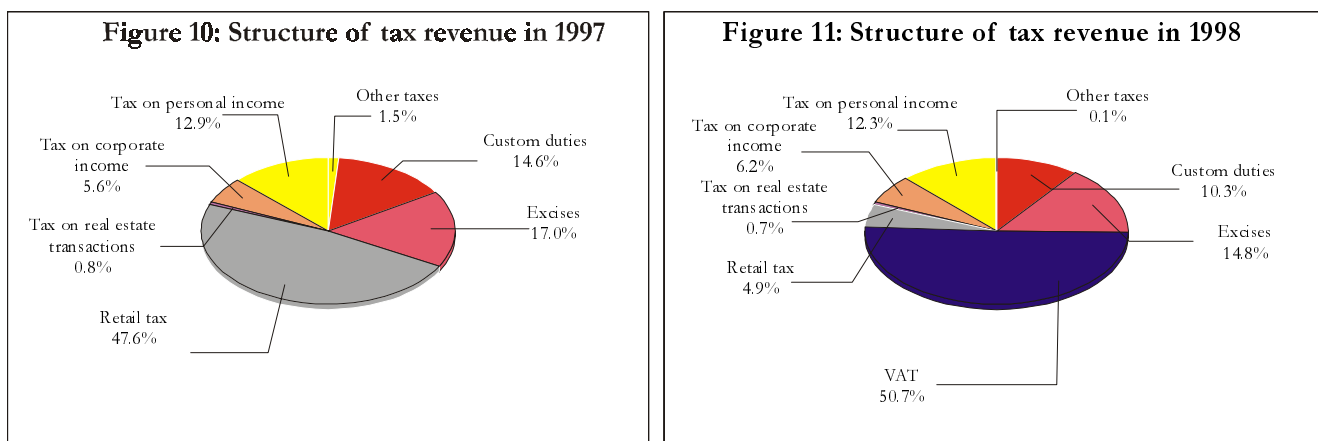


As presented by Figure 8, the share of tax revenues in total revenues continued with its downward trend in 1998. On the other hand, as shown by Figure 9, up to 1997 the share of tax revenues in gross domestic product lingered around 27 percent, reaching 29.66 percent in 1998 (the size of GDP as per data supplied by the SBS). Such an increase in the share of tax revenues in gross domestic product for 1998 primarily stems from a tax base extension and the taxation of certain segments of the grey economy following the introduction of value-added tax. While there are no reliable data for the structure of personal consumption, which might provide a firm reply to the question as to whether or not and, if yes, to what extent the introduction of VAT increased the tax burden to consumption, it should be mentioned that the standard sales tax rate used to be 26.5 percent, whereas the VAT rate has been set at 22 percent. Furthermore, bearing in mind the cumulative effect ensuing from the inability on the part of businesses to exclude, under the former sales tax system, all of the paid sales tax liabilities from their costs, it is clear that the VAT has not increased the incidence of taxation on consumption, which would explain such a sharp rise in the share of tax revenues in GDP. The increasing share of tax revenues in GDP results, in the first place, from more stringent tax discipline.



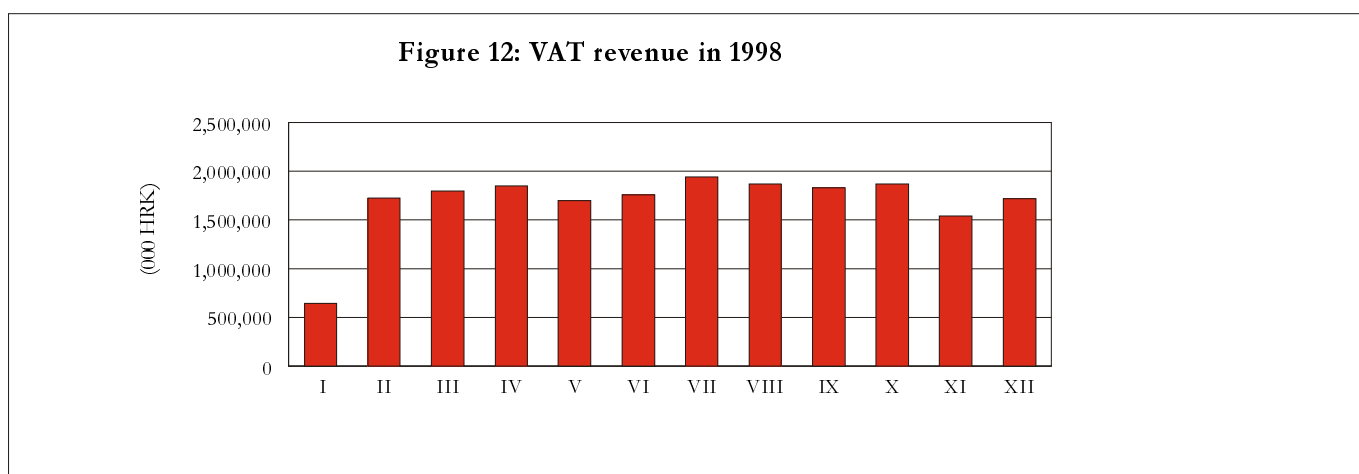
Source: Ministry of Finance and Central Bureau of Statistics for GDP data

The structure of tax revenues in 1997 and 1998 presented in Figures 10 and 11 shows the growing significance of the consumption and corporate profit taxes in the context of total revenues, whereas the share of excise taxes and customs duties is manifested in a downward trend.



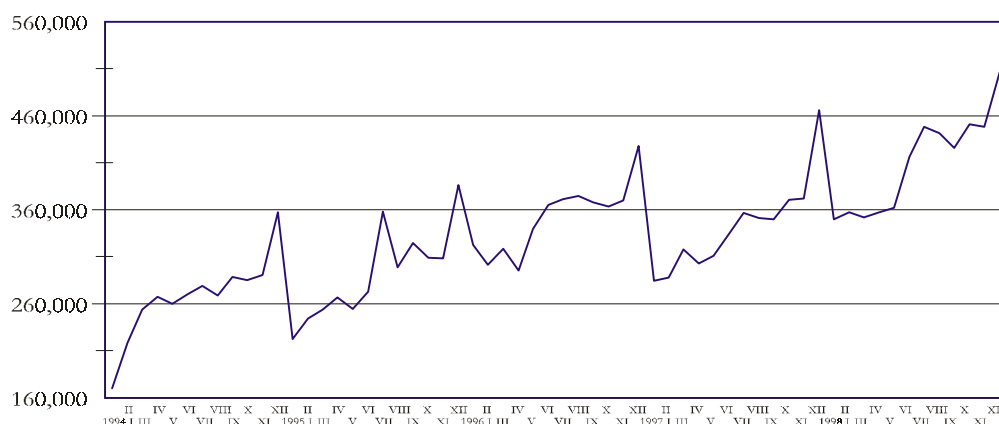
3.1.1. Value-added tax revenues

The major source of 1998 budget revenues was the value-added tax. Funds raised by means of the value-added tax amounted to HRK 20,228.2 million or 46.15 percent of total budget revenues. Figure 12 shows the monthly VAT trends, which indicate two facts. First, VAT revenues did not show any significant seasonality, at least during the first year of the VAT's application. The absence of any marked seasonal pattern in the VAT revenue trends may be ascribed to a one-off liquidity effect that resulted in exceptionally high revenues during the seasonally less productive first third of the year. However, any precise conclusion as to the seasonal pattern of VAT revenues will require a time sequence of five years at least. Secondly, the slackening of economic activity, which occurred in August 1998, had repercussions on revenue trends after October.



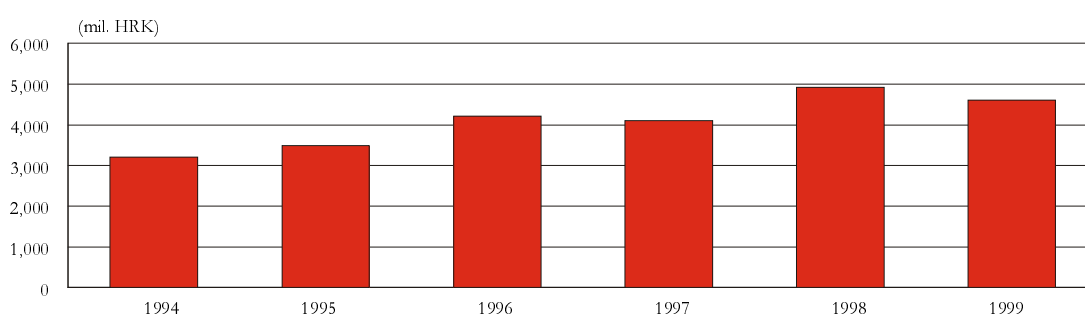
3.1.2. 1998 income tax revenues

Figure 13: Monthly revenue from taxes on personal income



The income tax⁴ revenues raised in 1998 were 19.8 percent above their 1997 levels. This ensued from a 12.6-percent rise in gross salaries during 1998, which also incorporates the effects of the abolishment of water supply and family allowance contributions, as a result of which gross salaries grew by approximately 2 percent. The monthly trends of income tax revenues are presented in Figure 13, while Figure 14 shows annual income tax revenues. Figure 13 clearly indicates that income tax revenues showed a seasonal upswing in July, August and December, due to the payment of additional salaries or holiday and Christmas grants and benefits. A downward trend evident in the 1997 annual revenues, as well as those planned for 1999, stems from reduced taxation incidence. In 1997, the lower taxation rate was decreased from 25 to 20 percent, while the non-taxable portion of income went up, with further increases in 1999.

Figure 14: Annual revenue from personal income tax



⁴In the Republic of Croatia, the income tax is assessed on the total income generated by each taxpayer within a (fiscal) year. Such total income may be reduced by losses carried forward, if any, and tax benefits of the taxpayer and his/her dependants. Pursuant to effective legislation, the income tax is assessed on any income earned as a result of employment or self-employment, and any income arising from property or property rights. The income taxation scale includes two tax rates. The first tax bracket is subject to a rate of 20%, while the second bracket pays at a rate of 35%. The limits of each tax bracket depend on the level of basic personal deduction. As of 1 January 1999, the basic personal deduction has been increased from HRK 800 to HRK 1,000. The income tax is assessed at the rate of 20% on the tax base up to the level of triple the basic personal deduction, which presently amounts to HRK 3,000 per month (HRK 36,000 p.a.). The 35% rate is applied to any portion of the tax base that exceeds that level. The personal deduction of pensioners amounts to HRK 2,500. In addition to the basic deduction, the level of personal deduction is also conditional by the number of dependants. Accordingly, the basic personal deduction is increased by appropriate coefficients.

In addition to this increase in income tax revenues, an upward trend has also continued in the number of income tax returns, particularly the number of requests for refunds of overpaid taxes. For 1997, a total of 401,304 taxpayers exercised their right to a tax refund, which constitutes a 31-percent increase over 1996. A total of HRK 380.2 million was refunded on account of taxes overpaid for 1997, while the additional payments of the income tax amounted to HRK 429.9 million, which means that net revenues generated as a result of annual income tax returns reached only HRK 49.8 million.

For 1997, small businessmen and the self-employed submitted fewer tax returns than they did for 1996, while the total and average income of these categories for 1997 increased by 9.76 and 10.74 percent respectively.

Table 2: Trends in the total number of tax returns

Description	Year			
	1994	1995	1996	1997
Number of tax returns processed	279,061	434,629	545,151	551,333
Additional tax payments according to annual tax returns (in HRK)	439,271,325	428,788,154	450,009,268	429,782,473
Tax refunds according to annual tax returns (in HRK)	83,153,172	213,214,231	341,912,452	380,295,790

Source: Ministry of Finance - Tax Department

Table 3: Tax returns submitted by small businessmen

Description	Year			
	1994	1995	1996	1997
Number of tax returns by small businesses	87,100	97,744	95,688	94,843
Total income of small businesses (in HRK)	1,507,610,699	2,668,726,880	2,903,691,525	3,187,225,351
Average income of small businesses (in HRK)	17,308,96	37,303	30,345	33,605

Source: Ministry of Finance - Tax Department

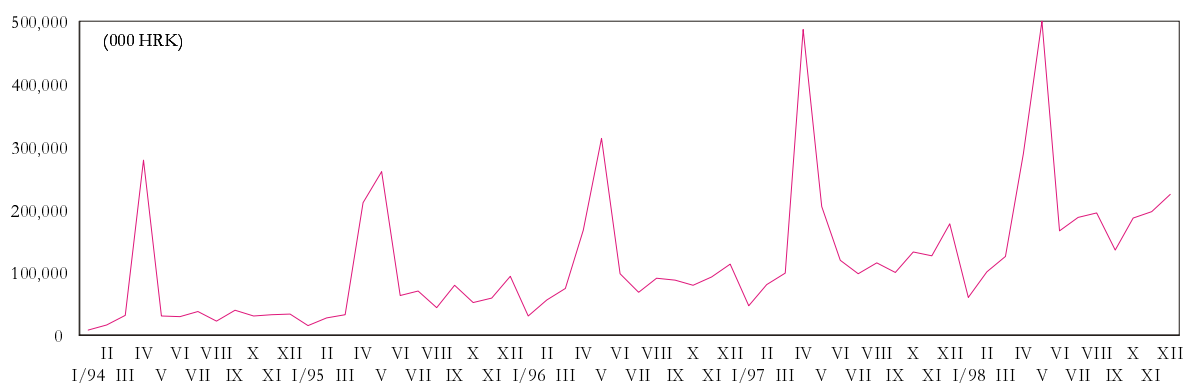
3.1.3. Corporate profit tax revenues

In the course of 1998, the profit tax⁵ continued to gain an ever-increasing importance as a source of budget revenues. The 1998 corporate profit tax revenues were as much as 37 percent above their 1997 levels, accounting for 5.6 percent of total revenues. The reason for such an increase in corporate tax revenues in the past few years certainly lies in the significant growth of economic activity, but also in improved tax discipline. Due to their concerns about the introduction of VAT at the beginning of 1998, local businesses intensified the issuance of invoices towards the end of last year, which also increased the payments of the corporate profit tax, since it is payable based on an invoiced value. It is quite clear that this phenomenon might affect the trends of corporate tax revenues for 1998, which will be paid to the Central Budget account during April and May 1999. However, as announced upon the adoption of the 1999 Budget, this is to be offset by an intensified control of taxpayers and more stringent fiscal discipline. In addition, as 1998 saw a reduction in producer prices, a 5-percent protective interest will be applied in the calculation of the corporate profit tax for 1998. In 1998, the protective interest rate was 7.3 percent. The monthly trends of corporate profit tax revenues are presented in Figure 15, which clearly indicates a marked seasonal character of revenues from this source.

Taxpayers with one child multiply their basic personal deduction by the coefficient 1.5 (1.5*1,000), the coefficient for taxpayers with two children is 1.7, for those with three children it is 2.0, and for each additional child the coefficient is progressively increased.

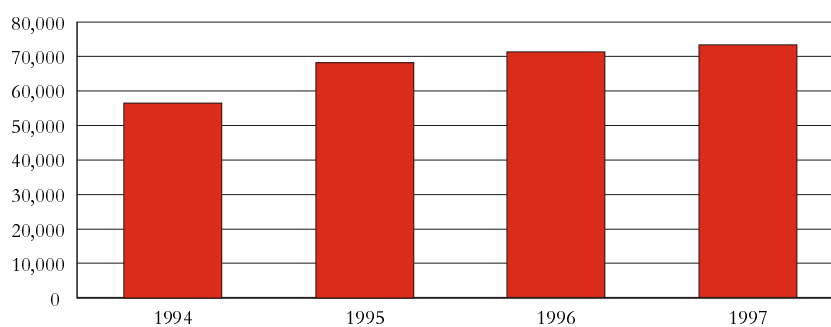
⁵As of the beginning of 1997, the corporate profit tax rate has been set at 35%. One of the specific features of Croatia's corporate profit tax is the existence of protective interest. The tax basis is reduced by the amount of this protective interest. Its purpose is to ensure the economic neutrality of the corporate profit tax, that is, to place investments in real and financial assets on an equal footing. The protective interest rate has been set at 5%, plus the annual growth rate of producer prices. The corporate profit tax is advanced on a monthly basis, pursuant to the tax return for the previous year, while the final tax return for the preceding year must be submitted by April of the current year.

Figure 15: Monthly revenue from corporate income tax



In 1998, a total of 73,323 corporate profit tax returns were received for 1997, which is a 2.8-percent increase in year-on-year terms.

Figure 16: Number of registered profit tax returns



In 1998, the Ministry of Finance continued with its practice of granting awards to the best and most orderly taxpayers. The list of the awarded taxpayers is presented in Table 4.

Table 4: Outline of the greatest taxpayers in 1997

Tax payers of corporate income tax	Tax payers of personal income tax
Pliva d.d., Zagreb	Stjepan Šimunković, Čabar, construction
Ericsson-Nikola Tesla d.d., Zagreb	Miroslav Mamić, Kaštel Lukšić, sales
Tvornica duhana Rovinj d.d., Rovinj	Marijan Ritoša, Poreč, carpenter
Karlovačka pivovara d.d., Karlovac	Mirjana Borić, Belišće, public notary
Heruc d.d., Zagreb	Jelena Marčinković, Sisak, construction
Čakovečki mlinovi d.d., Čakovec	Kata Marošević, Županja, technical services
Combis d.o.o., Dubrovnik	Mato Baričević, Zagreb, plastics
Chromos-svjetlost d.d., Lužani	Mirko Šargač, Novi Marof, chicken farm
MG Tehnoplín d.d., Lipik	Ivan Kračun, Pregrada, gas, water, heating installation
Graditelj d.d., Otočac	Ljubo Šarunić, Zadar, pharmacy

Source: Ministry of Finance - Tax Department

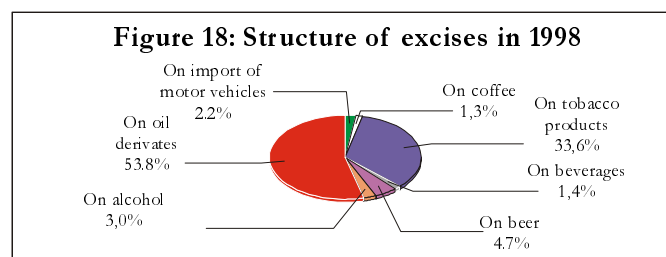
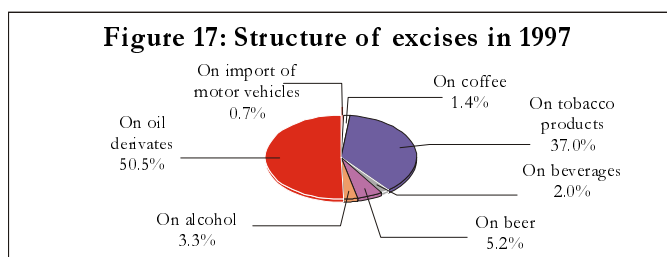
3.1.4. 1998 excise tax revenues

Special duties or excise taxes constitute charges payable in an absolute amount, as per measure unit of the product. The introduction of excise taxes in the taxation system of the Republic of Croatia commenced as early as July 1993, with the introduction of an excise tax on coffee. A year later, that is, in July 1994, excise taxes were levied on petroleum products, tobacco and tobacco products, alcoholic beverages, beer, soft drinks and imported cars. These taxes are marked by the simplicity of collection, a small number of taxpayers and abundance. In addition to becoming an important source of central budget revenues, these taxes have been introduced in an attempt to achieve the progressiveness of Croatia's tax system. The trends of excise tax revenues are presented in Table 5, which shows that this type of taxes from one year to another gains an ever-increasing importance.

Table 5: Revenues from Excises

	Outturn					Budget
	1994	1995	1996	1997	1998	1999
Total excises taxes	1,854,815	4,960,440	5,390,785	5,404,837	5,896,787	6,619,597
on oil derivates	670,441	2,559,021	2,691,840	2,728,346	3,169,770	3,626,685
on alcohol	75,140	183,458	197,623	176,681	176,897	200,927
on beer	128,983	266,031	262,080	279,086	277,889	331,097
on beverages	51,208	108,498	108,737	110,255	83,182	96,701
on tobacco products	880,466	1,759,266	2,039,532	1,999,988	1,983,435	2,139,242
on coffee	41,234	67,642	68,704	74,959	76,807	85,094
on import of motor vehicles	7,343	16,524	22,269	35,522	128,806	139,851

Source: Ministry of Finance - Tax Department



Among special duties, the major source of revenues generated in 1998 is the excise tax on petroleum products, whose monthly trends are shown in Figure 19. This tax accounted for more than 50 percent of total revenues from special duties or 7.94% of total tax revenues. The assessment basis of this tax is one litre or kilogram of the manufactured or imported petroleum product⁶.

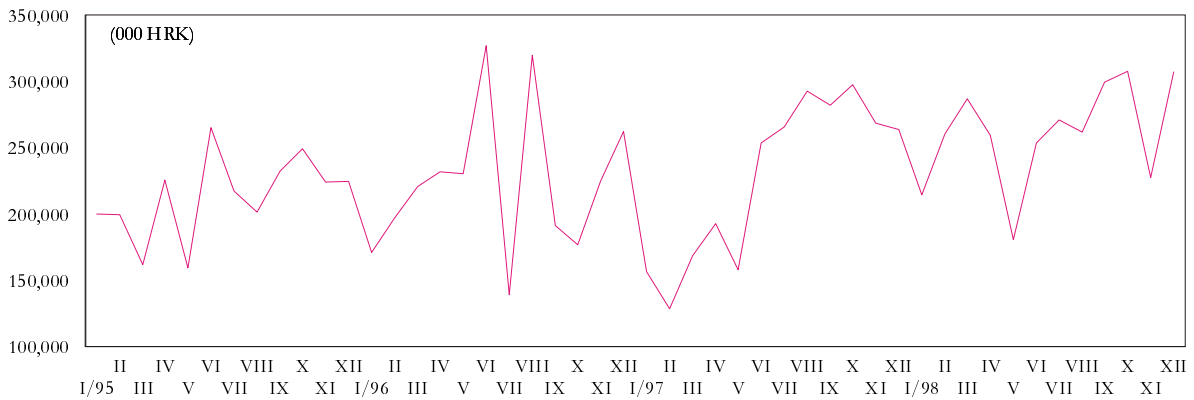
⁶ The special tax on petroleum products is paid per litre of:

- motor petrol MB-98 - HRK 1.90;
- unleaded motor petrol (BMB) - HRK 1.60;
- diesel fuel - HRK 1.40;
- heating oil - HRK 0.30;

The special petroleum products tax is paid per kilogram of:

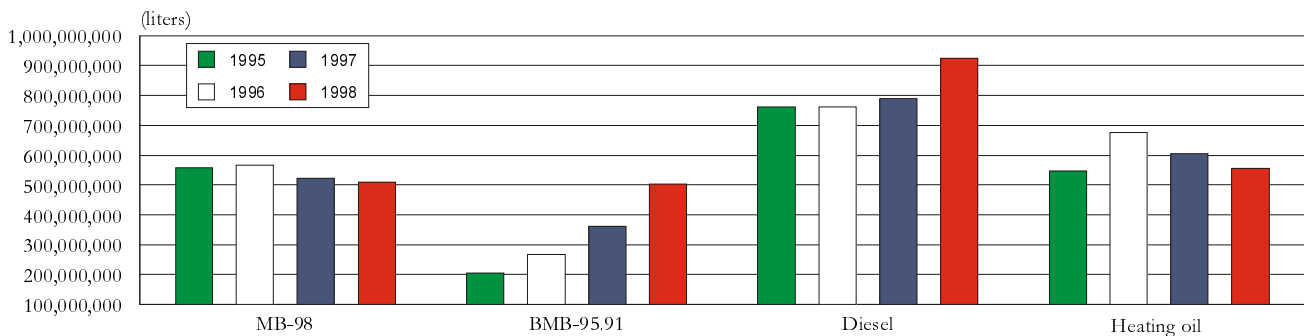
- paraffin - HRK 1.4;
- liquefied petroleum gas - HRK 0.10.

Figure 19: Monthly revenue from excises on oil derivatives



As shown by Figure 20, the taxable quantities of petroleum products supplied in 1998 increased 9 percent. A considerable increase in taxable quantities has been reported for unleaded petrol and diesel fuel, while the quantities of MB-98 motor petrol and heating oil slightly decreased. Also, there occurred a decline in the share of imported petroleum products in total quantities supplied. As a result of such trends in quantities supplied during 1998, the revenues from this source increased 16 percent over 1997.

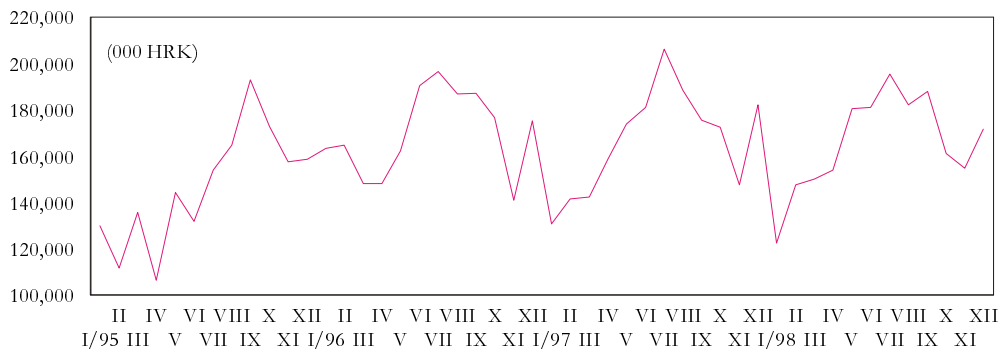
Figure 20: Taxable quantities supplied to domestic market



The excise tax on tobacco products⁷ accounted for 33.6 percent of total excise tax revenues. The monthly trends of revenues from the excise tax on tobacco products in 1998 are presented in Figure 21. However, the 1998 revenues from the excise tax on tobacco products are 0.7 percent below their 1997 levels, which stems from a 1.5-percent decrease in quantities supplied in 1998.

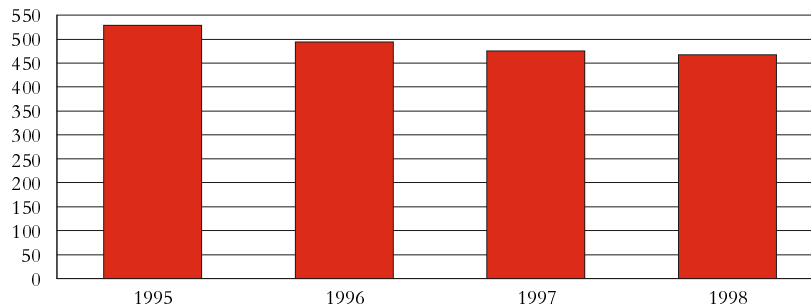
⁷The tax base for this tax are domestic and imported cigarettes and other tobacco products. The tax bases for this tax are as follows: for cigarettes - a pack of 20 cigarettes of a standard length of 84 mm; for tobacco - 1,000 grams; for cigars - per piece; and for cigarillos - a 20-piece pack. The special duty on cigarettes ranges from HRK 3.50 for domestic cigarettes in soft packs to HRK 8.50 for imported cigarettes. The tax payable on imported tobacco is HRK 56.00, and that paid on domestic tobacco amounts to HRK 28.00 per kilogram. HRK 0.60 per unit is paid for cigars, and HRK 0.40 per pack for cigarillos.

Figure 21: Monthly revenue from excises on tobacco products



Other excise taxes - notably, those on alcoholic beverages, soft drinks, beer, coffee and imported motor vehicles - generated 12.6 percent of total excise tax revenues in 1998⁸. Among other excise taxes, the most significant is that on the imports of motor vehicles. This tax is imposed on the imports of cars, motorcycles, vessels and aircraft. The 1998 revenues from the excise tax on motor vehicles were two and half times higher than a year ago. Such an upswing of this revenue item ensues, as indicated by import data, from significant imports of cars, but also from an extension of the tax basis for this import. Namely, up to 1998 this tax was imposed only on imports of new automobiles and, since 1 January 1998, it has also been applied to other motor vehicles, including used vehicles.

Figure 22: Domestic and imported cigarette packages sold (in million of packages)



⁸As of 1 January 1998, the excise taxes on domestic and imported beer have been equalised and set at HRK 80.00 per hectolitre of alcoholic beer, and HRK 40.00 per hectolitre of non-alcoholic beer. At the same time, equal treatment has been introduced for imported and domestic soft drinks, and the taxation rate has been set at HRK 40.00 per hectolitre since the beginning of 1998. The excise taxes on imported and domestic alcoholic drinks were levelled more recently. Namely, since 1 January 1999 the excise tax per litre of absolute alcohol, at a temperature of 20 centigrade, has been set at HRK 40.00, irrespective of its origins. This levelling is in compliance with the requirements of the World Trade Organisation for equal tax treatment of domestic and imported products on the local market.

3.1.5. Custom revenue in 1998

Customs revenues in 1998 dropped by HRK 550 million as compared to 1997, that stems from more liberal trade with Slovenia, Bosnia-Herzegovina and Macedonia, but also from a decline in imports. As explained in detail in the introductory chapter on macroeconomic trends, total imports shrunk by 8.2 percent during 1998. However, this 8.2-percent decrease in total imports arises from trends in three segments: commodity imports, imports involving processing and other imports. The major agent of such trends in customs revenues is commodity imports, which declined by as much as 7.9 percent. Of course, the 1998 trends in imports - and, consequently, customs revenues - also reflect the absence of any effect of the introduction of the VAT, which triggered off a one-shot raise in imports back in 1997. Expectations for Croatia's impending admission to WTO membership provide another reason for the further decline in the importance of customs revenues.

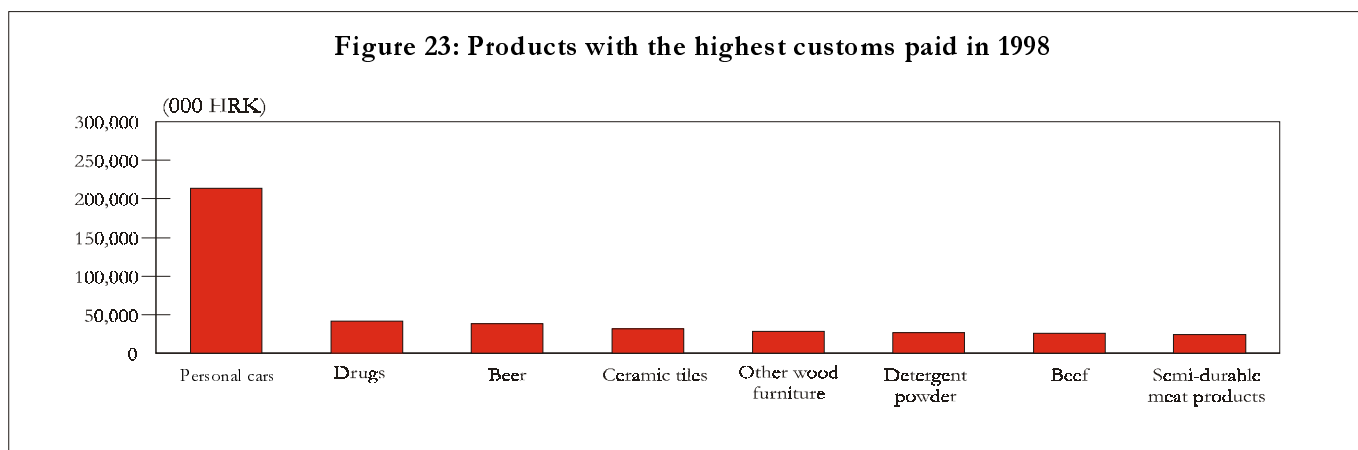
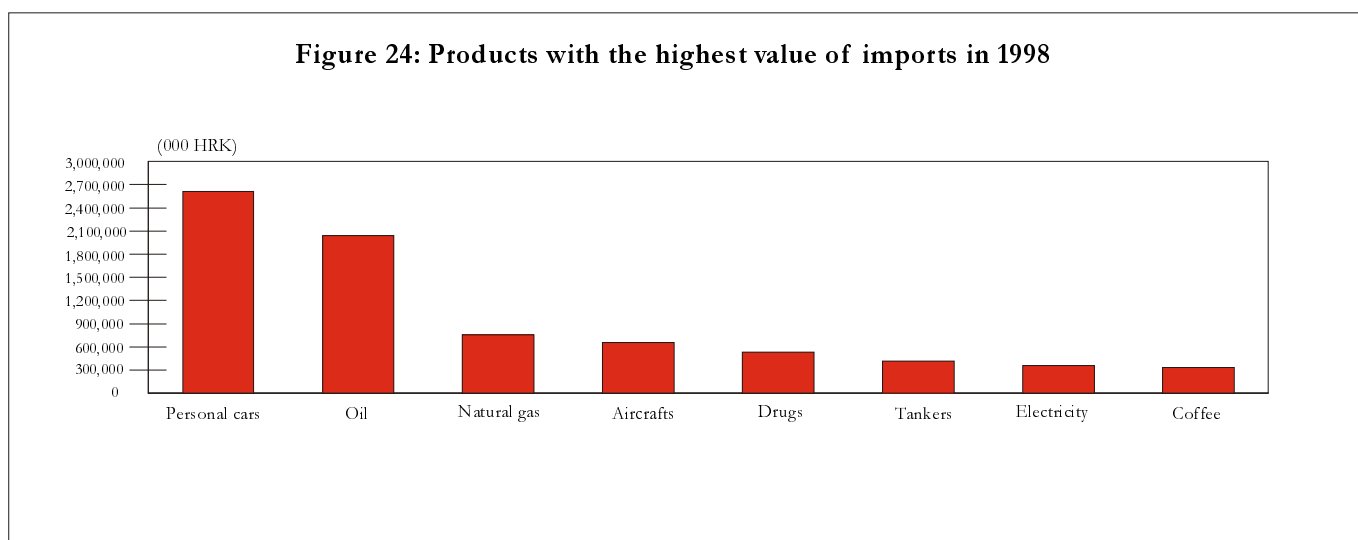


Figure 23 presents products with the highest levels of customs duties collected, while Figure 24 shows products with the highest import values in 1998.



3.2. NON-TAX REVENUES

The structure of non-tax revenues in 1997 and 1998 is presented in Figures 25 and 26. A marked decrease in the share of revenues from road fees in total non-tax revenues results from the shift of these proceeds to the level of local government. The strongest year-on-year growth has been recorded under the item of other property revenues, which increased from HRK 83.5 million in 1997 to HRK 239 in 1998. Proceeds from the surplus of the CNB's income over its expenses more than doubled as compared to 1997, reaching HRK 265.1 million. Central budget revenues from a portion of profits generated by public enterprises in 1998 increased by 6.45 percent in year-on-year terms.

Figure 25: Structure of nontax revenue in 1997

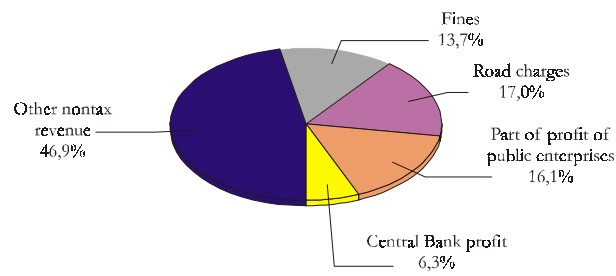
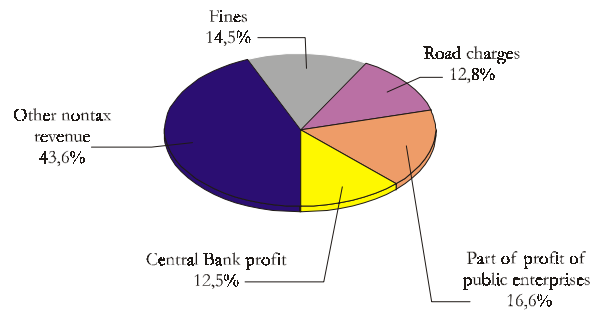


Figure 26: Structure of nontax revenue in 1998



3.3. CAPITAL REVENUES

Capital revenues accounted for approximately 4 percent of total budget revenues in 1998. In the preceding years, except for 1996, the share of these receipts was much lower. The level of capital revenues in 1998 results from the disposal of a portion of the government's share in the pharmaceutical company Pliva. It should be noted that Pliva's public offering should have taken place as early as October 1997. However, due to the collapse on international stock markets in October 1997, it was impossible to realise this transaction under conditions acceptable to Croatia, and the deal was postponed at the last moment. Apart from privatisation proceeds, capital revenues also include receipts from the sale of state-owned and military flats and proceeds from the disposal of state-owned land. In aggregate terms, the sale of state-owned and military flats accounted for 19.9 percent of total capital revenues, which is a 12.3-percent increase over 1997.

4. 1998 CENTRAL BUDGET EXPENDITURE OUTTURN

The 1998 central budget expenditure amounted to HRK 42,551.9 million or 21.55 above the 1997 outturn, but 4.6 percent below the planned level. With total revenues amounting to HRK 43,808.6 million, as described in detail in the preceding section, the 1998 budget surplus totalled HRK 1,256.7 million. The government's current savings amounted to HRK 7,136.4 million, which equals the excess of current revenues over current expenses.

Figure 27: Structure of central government expenditures in 1997

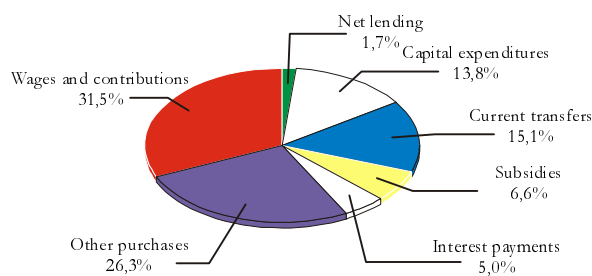


Figure 28: Structure of central government expenditure in 1998

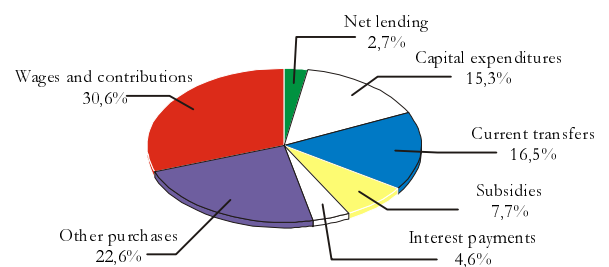


Table 6: Central government budget expenditure

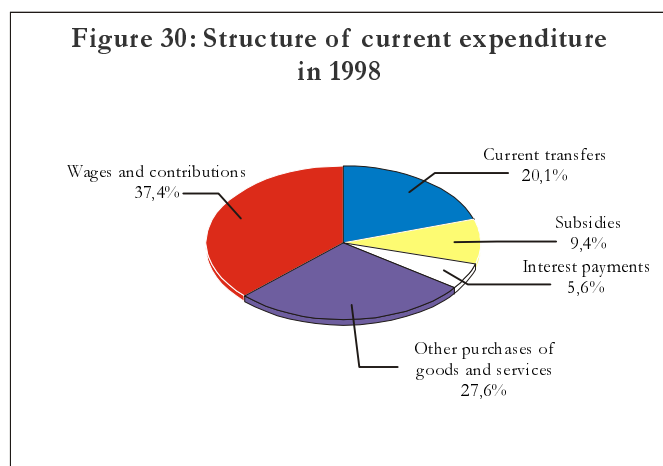
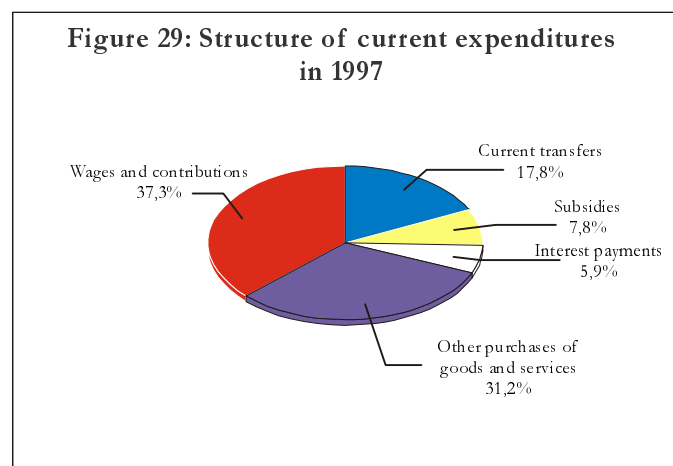
(000 HRK)	Budget 1998	Revised Budget 1998	Outturn 1998
Total expenditure and lending minus repayments	39,134,564	44,596,194	42,551,916
Expenditures on goods and services	21,700,193	22,803,087	22,648,712
Interest payments	2,572,250	2,505,889	1,951,283
Subsidies	2,380,324	3,059,593	3,274,689
Transfers	5,335,428	7,282,410	7,008,342
Capital expenditures	5,489,182	7,283,828	6,507,346
Lending minus repayments	1,657,187	1,661,387	1,161,544

Source: Ministry of Finance

4.1. CURRENT EXPENSES

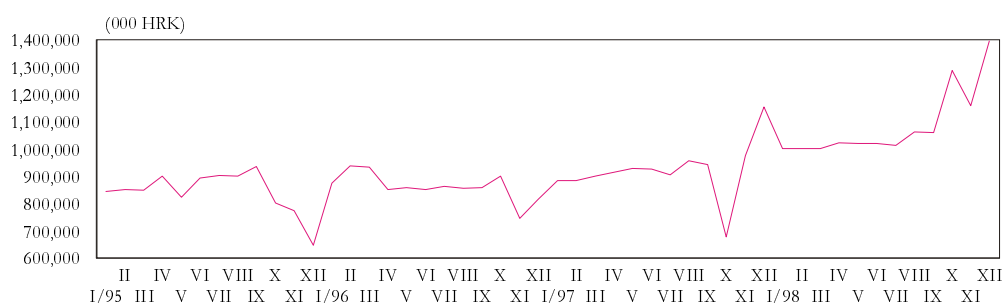
In 1998, current expenses were HRK 34,883.02 million, or 97.85 percent, of their planned level. Figure 30 clearly shows that outlays for the salaries of budget beneficiaries account for the major share in total current expenses. We can also see the already mentioned year-on-year increase in the share of subsidies and current transfers in aggregate current expenses.

In 1998, expenses for the gross salaries of central budget beneficiaries amounted to HRK 13,030.3 million, which is 1.14 percent above the revised planned level, and 18.03 percent in excess of the amount spent in 1997.



With a view to reducing the gap between the salaries of civil servants and those earned by officers and employees in other services, the salaries of central budget beneficiaries were raised on three occasions during 1998. The first increase took place in January, when the salaries went up by 7 percent. In August, they were raised by 8 percent, followed by a 10-percent increase in November. In December, central budget users also received so-called Christmas bonuses amounting to HRK 1,000 per person, together with a HRK 400 cash donation for children. In pursuit of the mentioned goal to level salaries, an agreement on a 17-percent raise in salaries has been reached for 1999. This increase should be realised in two stages, first in August, when the salaries will go up by 5 percent, and then in December, when they will rise by an additional 12 percent. The concluded collective agreement also provides for Christmas bonuses and donations for children equal to those paid in 1998.

Figure 31: Gross wages of the budget users



Expenses for the purchase of other goods and services in 1998 increased by 4.28 percent in year-on-year terms. Current defence expenses accounted for 40 percent of this expenditure item, with a year-on-year growth of 6.53 percent. Together with law enforcement and public safety expenses, the share of defence spending in total expenditures for the purchase of other goods and services reached 45.85 percent in 1998, or 2.06 percent above its 1997 level. We can also see a 25.11-percent year-on-year drop in welfare expenses for displaced persons and refugees, whose share in total expenditure for the purchase of other goods and services reached 6.23 percent in the year under review.

In 1998, interest payments increased by 12.34 percent over 1997, and are almost equally distributed between domestic and foreign creditors. Namely, in 1998 domestic creditors received interest payments amounting to HRK 917.3 million, while interest paid to foreign creditors reached HRK 1,033.9 million.

Figure 32: Structure of interests payments in 1997

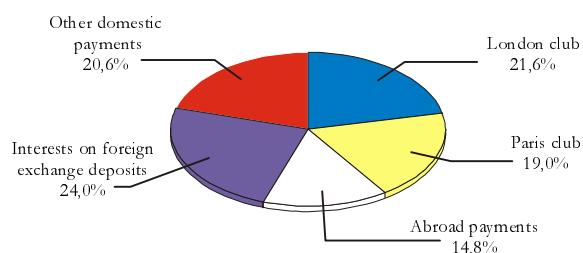
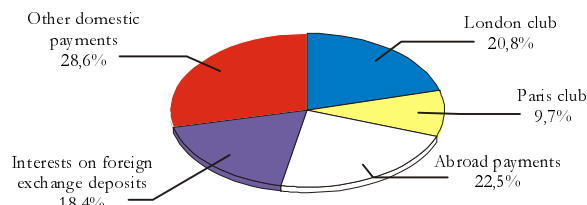


Figure 33: Structure of interest payments in 1998



Subsidies granted and current transfers made in 1998 grew by 35.67 percent over their 1997 levels. In 1998, total funds spent for subsidies increased 41.94 percent in comparison to 1997. The major beneficiary of subsidies was the Croatian Railway Company, which received HRK 1.6 billion, followed by agriculture, which was granted HRK 1,044.8 million or 83.3 percent more than in 1997, the tourist industry with HRK 190 million and the restructuring of economy with HRK 208.7 million. In 1998, the Central Budget also subsidised Jadrolinija, Lošinjska plovidba, Rapska plovidba, Dunavski Lloyd and Mediteranska plovidba (local shipping companies), and the ports of Rijeka, Ploče and Vukovar.

Figure 34: Structure of central budget subsidies in 1997

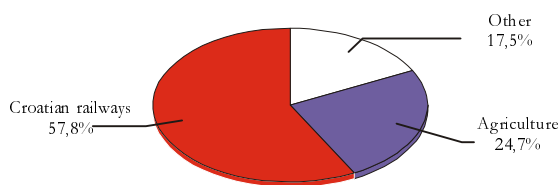
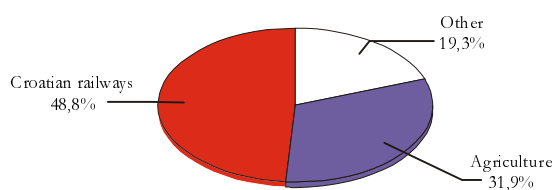


Figure 35: Structure of central budget subsidies in 1998



The 1998 current transfers increased by 32.93 percent in year-on-year terms, and were mostly directed towards extra-budgetary funds that were exerting major pressure on central budget expenditure throughout the year. The structure of current transfers is presented in Figures 36 and 37. Transfers made to the Pension Insurance Institute in 1998 amounted to HRK 3,837 million or 46.25 percent above their 1997 levels. A total of HRK 1,467 million was transferred in excess of the original budget of this extra-budgetary fund and HRK 556.1 million in excess of levels planned in the revised budget. The strongest year-on-year increase - 99.5 percent - was reported for transfers made to the Croatian Health Insurance Institute. This Institute received transfers totalling HRK 1,561.03 million, including capital transfers of HRK 593 million. Total current transfers to the Health Insurance Institute amounted to HRK 972.8 million and were HRK 52.3 million above their levels as planned in the revised budget. Following the abolishment of children's allowance and water tax contributions in June 1998, the required funds were allocated from the Central Budget until the end of the year, in accordance with amounts provided for in the revised budget. Accordingly, a total of HRK 502.2 million was allocated for children's allowances, while transfers to the public Water Company amounted to HRK 135 million. In 1998, total transfers made from the Central Budget to the public Water Company reached HRK 318.4 million or 3.41 percent above their 1997 levels. The 1998 transfers to non-profit organisations amounted to HRK 356.6, which is a 13-percent increase over the preceding year. They mostly went for subsidised student room and board (HRK 180 million). Among transfers to the general population, support for Homeland War veterans constitutes the major item, amounting to HRK 768.2 million or nearly 86.39 percent of total transfers to general population.

Figure 36: Structure of current transfers from central budget in 1997

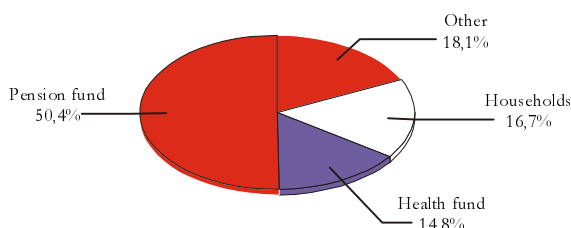
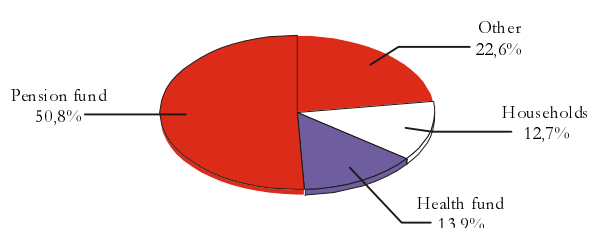


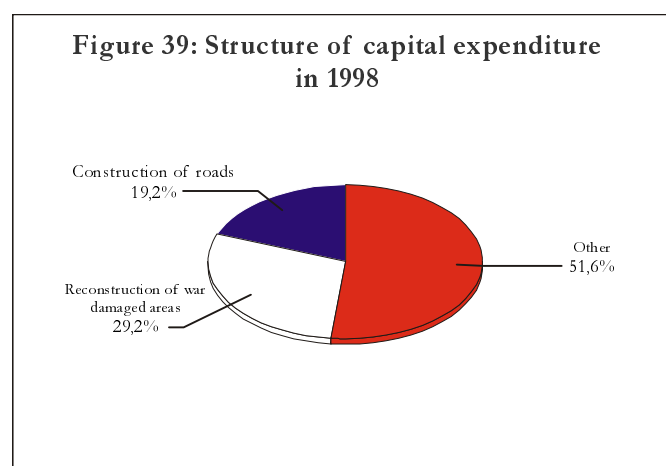
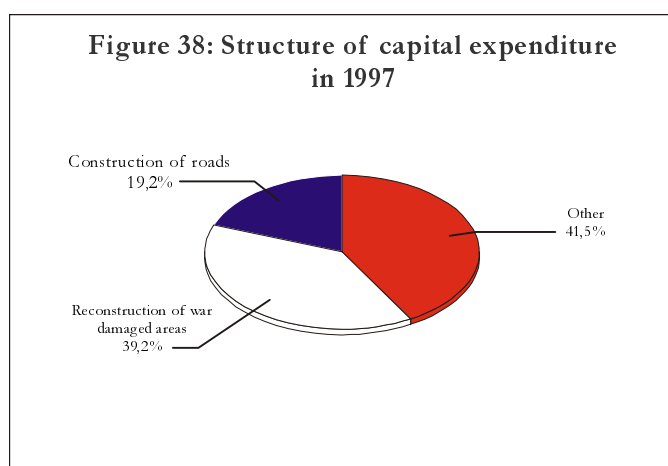
Figure 37: Structure of current transfers from central budget in 1998



4.2. CAPITAL EXPENSES

Capital expenses incurred in 1998 reached 89.34 percent of their levels planned in the revised budget or 35.13 percent above their 1997 levels. The major portion of these funds was spent for road construction and maintenance: HRK 1,200.0 million or 29.6 percent in excess of the amount spent in 1997. In 1998, HRK 875 million was allocated from the Central Budget, whereas foreign loans provided funds for the remaining HRK 325 million. In the past three years, capital expenses in the Republic of Croatia reached an average of 5.7 percent of the registered GDP, which reflects major government investments caused, in the first place, by the

reconstruction of war-damaged areas and the aforementioned outlays for the development of road infrastructure.



The 1998 expenditures for capital transfers increased by 32.91 percent over their 1997 levels, amounting to HRK 3,454.5 million. The previously mentioned capital transfers to the Croatian Health Insurance Institute (HRK 593 million) and the Croatian water management administration (HRK 172.9 million) accounted for nearly one fourth of total expenses for capital transfers in 1998, while reconstruction expenditures constituted 38.04 percent.

4.3. NET BORROWING

In the course of 1998, net borrowing was mostly allocated for the reconstruction of the water supply and utilities infrastructure, as well as the infrastructure of the Croatian Railway Company and the rehabilitation of Dubrovačka banka. In 1998 HRK 601 million was spent for the rehabilitation of this bank, which became 100-percent state-owned.

4.4. FUNCTIONAL CLASSIFICATION OF GOVERNMENT EXPENDITURE

The functional classification reflects the allocation of central budget funds, irrespective of differing economic characteristics of particular expenses meeting one and the same requirement.

Therefore, the functional classification indicates total costs incurred throughout a year for the provision of particular categories of public services.

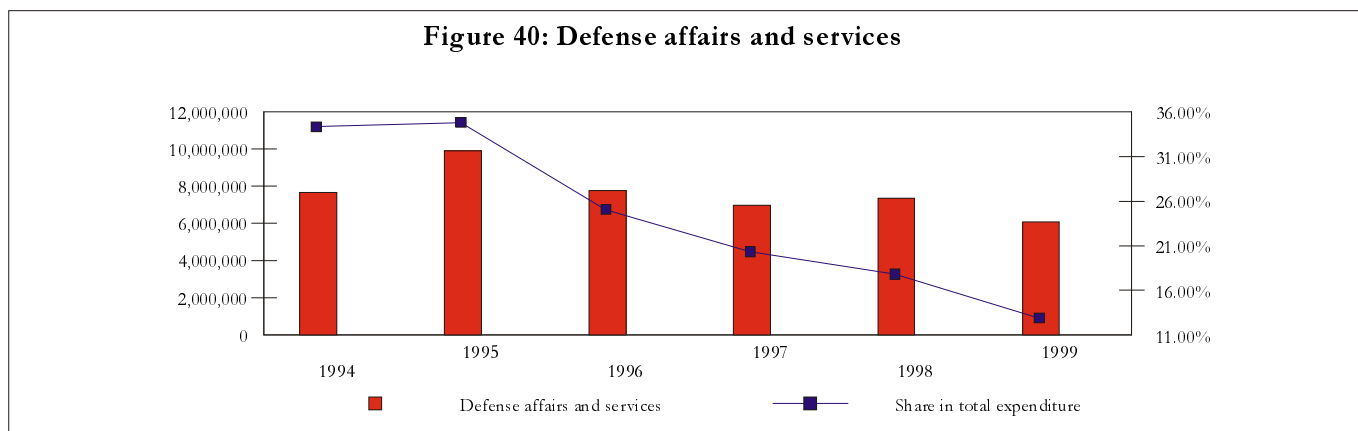
Table 7: Budgetary Central Government Expenditure by Function, share in total expenditure

(in %)		Outturn	Outturn	Budget
		1997	1998	1999
I.	Total expenditure	100	100	100
1.	General public services	6.35	8.17	7.88
2.	Defence affairs and services	20.32	17.81	12.88
3.	Public order and safety affairs	12.12	10.27	9.73
4.	Education affairs and services	11.78	11.28	12.56
5.	Health affairs and services	0.54	1.97	1.76
6.	Social security and welfare affairs and services	18.76	19.39	23.07
7.	Housing and community amenity affairs and services	6.02	6.33	5.76
8.	Recreational, cultural and religious affairs	1.57	1.39	2.00
9.	Agriculture, forestry, fishing, hunting affairs	1.79	2.67	2.46
10.	Mining, manufacturing, construction affairs	2.01	1.76	1.02
11.	Transport and communication affairs and services	9.98	9.84	11.65
12.	Other economic affairs and services	1.89	1.33	1.73
13.	Expenditures not classified by major group	6.87	7.79	7.50

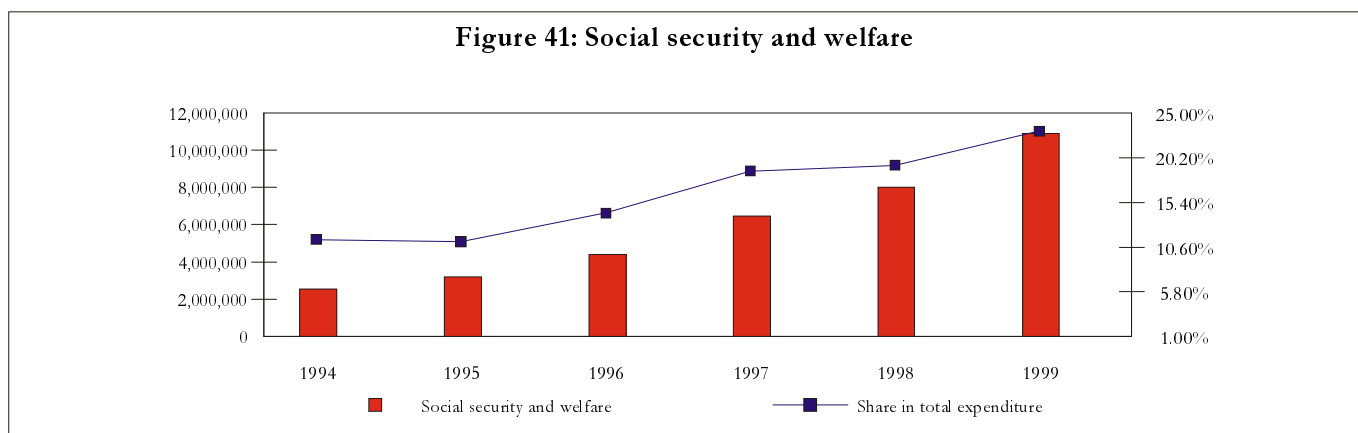
Source: Ministry of Finance

Table 7 shows the breakdown of actual central budget expenses as per their functional classification in 1998. While defence projects still draw considerable funds, their share in total budget expenses shows a downward

trend and indicates a change in the overall budget structure in favour of civil requirements. In 1998, defence spending accounted for 17.81 percent of total budget expenditure, as compared to not less than 34.81 percent in 1995. Taken together with law enforcement and public safety expenses, the share of defence spending in total expenditure plummeted from 47.08 percent in 1994 to 28.08 percent in 1998. Figure 40 clearly shows this downward trend in defence expenses.

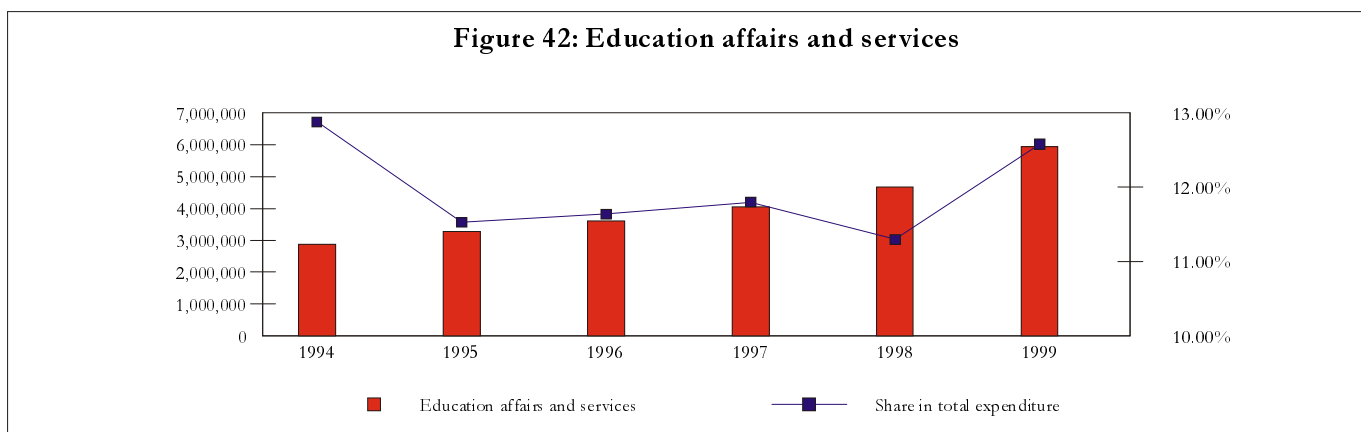


Although its share in GDP also shows a downward trend, defence spending still stands at 6 percent of GDP, which is quite high in comparison with other countries. Namely, in 1995 defence expenditures accounted for 10.07 percent of GDP. On the other hand, in the period from 1985 to 1995 the developed OECD countries allocated an average of 2 percent of their GDPs for defence. However, this international benchmarking must be viewed with certain reservations, since Croatia is a young country which has yet to fully establish its military force and which borders a politically very unstable region. For these reasons, defence expenses should not be expected to fall in the foreseeable future on a level existing in other European countries, but we can expect that this expenditure item will continue to show a downward trend.



This shrinking share of defence, law enforcement and public safety expenses is paralleled by increasing outlays for social insurance and welfare services, which have become the major budget expenditure item. Such a trend in social insurance and welfare expenses reflects the previously described increase in various forms of current transfers. The 1999 budget for social insurance and welfare services is 35.8% above the amount actually spent in 1998. In relation to 1994, the level of funds to be allocated for social insurance and welfare services in 1999 has increased by 328%, which clearly testifies the attention paid by the Central Budget to providing for the most vulnerable segments of the society. Trends in social protection and welfare expenses are presented in Figure 41.

Figure 42: Education affairs and services



Services whose significance should certainly grow with more intensity are those related to education, including pre-school, primary, secondary and university education. In the past few years, the average share of education expenses in BDP has been standing at 2.4 percent, as compared to 5 percent reported by the developed OECD countries. Indeed, certain improvements towards increasing education expenses, which are - under contemporary conditions - no longer treated as costs but rather as priority investments in future growth and development, have been observed in 1999. However, if Croatia is to develop more rapidly, education expenses must also grow with more intensity, for this is the only way to ensure the country's future prosperity.

III. PUBLIC DEBT OF THE REPUBLIC OF CROATIA IN 1998

1. CREDIT RATING OF THE REPUBLIC OF CROATIA

Four credit rating agencies evaluated the credit rating of the Republic of Croatia: Moody's Investors Service, Standard & Poor's Corporation, Fitch IBCA and R&I. A credit rating review is presented in Table 1.

The Moody's Investors Service, Standard & Poor's Corporation and Fitch IBCA evaluated the credit rating of the Republic of Croatia for the first time at the beginning of 1997, when Croatia obtained an investment credit rating.

At the end of 1997, the Republic of Croatia also requested that the Japanese agency R&I estimate its credit rating, and obtained an investment credit rating (BBB), which was one point higher than the grade obtained from above-mentioned agencies.

All of the aforementioned agencies conduct their regular annual verification of the given credit ratings. In 1998, such verifications resulted in the confirmation of the investment credit rating, whereas this year's regular credit rating verification is still in progress.

On February 24 1999 Croatia obtained a grade (Baa1) by Moody's Investors Service for long-term domestic borrowings, which is two points higher than the grade for long-term foreign borrowings, obtained by the same agency, and it corresponds to the credit ratings obtained by Standard & Poors and Fitch IBCA for long-term domestic borrowings.

Table 1: Review of the credit ratings of the Republic of Croatia

	Long-term credit rating Foreign currency	Long-term credit rating Domestic currency	Short-term credit rating Foreign currency
Mood's Investors Service	Baa3	Baa1	P-3
Standard & Poor's	BBB-	BBB+	A3
Fitch IBCA	BBB-	BBB+	A3
R & I	BBB		

Source: Ministry of Finance

2. PUBLIC INTERNAL DEBT IN 1998

A detailed category description of internal debt is shown in the "Annual Report of the Finance Ministry 1994-1997", so that here only newly formed debt categories in 1998 are described in much detail. It should be stressed that almost all internal debt categories are bound to the currency clause on the German mark exchange rate (i.e. the Euro) meaning that the comparison of conditions at the end of 1997 and 1998 also contains the effect of exchange rate depreciation. The internal debt structure is shown in Table 2. The depreciation programme for internal debt is shown in Table 3, whereas Table 4 shows the internal debt position as a result of the depreciation programme.

The new internal debt category, which emerged during 1998, was bonds issued by the State Bank Rehabilitation Agency during the process of rehabilitation and restructuring of Dubrovačka banka Dubrovnik - DAB V (Dubrovačka banka)⁹.

The DAB V series bonds were issued in the amount of HRK 1,000.5 million against the currency clause (equivalent amount in DM according to the mean exchange rate of the Croatian National Bank (CNB) on 31 December 1997) with an interest rate of 6 percent and 10 year maturity date. These bonds should have been paid off every six months on May 15 and October 15. 534 million of the total amount of the bonds issued in accordance with the Decision were intended to cover losses, which could not be charged off on equity capital, whereas the remaining HRK 467.5 million will be used for the bank's necessary additional capital investments.

⁹ Decision on the Rehabilitation and Restructuring of Dubrovačka banka d.d. Dubrovnik, Official Gazette (*Narodne novine*) No. 56/98

Table 2: Domestic debt of the Republic of Croatia in 000 HRK

Debt item*	December 31, 1997	December 31, 1998	Maturity:	Interest rate:
Frozen foreign exchange deposits	7,093,300	6,424,805	2005	5.00%
Big Bonds - Series I	1,462,620	1,463,408	2011	
Big Bonds - Series II	744,170	746,047	2011	7.20%
Big Bonds - Series III	722,171	736,385	2012	7.20%
Big Bonds - Series IV	643,600	433,774	2000	12.00%
Bond JDA	270,590	95,799	1999	12.00%
Bond JDB	345,300	183,370	1999	8.00%
Reconstruction Bond	19,320	22,818	2003	7-10%
Eurokuna	300,000	0	1998	12.50%
BRA Bonds I	1,084,600	1,064,173	2007	6.00%
BRA Bonds II	297,380	300,681	2012	5.00%
BRA Bonds III	756,310	747,327	2012	7.20%
BRA Bonds IV	419,780	411,585	2012	5.00%
BRA Bonds V-A		405,680	2008	6.00%
BRA Bonds V-B		-	2008	7.00%
Medium and long term debt	14,159,141	13,035,852		
Treasury Bills	449,600	565,800		
Other short-term debt	0	0		
Short-term debt	449,600	565,800		
Total debt	14,608,741	13,601,652		

Source: Ministry of Finance

*Detailed description of debt categories is given in the "Annual Report of the Ministry of Finance 1994 - 1997"

Table 3: Internal debt amortisation (HRK millions)

	1998	1999	2000	2001	2002	2003	2004	2005
Amortisation	2,259.79	2,057.47	1,676.94	1,550.87	1,579.70	1,610.45	1,643.32	1,171.52
FFED	1,005.08	1,005.08	1,005.08	1,005.08	1,005.08	1,005.08	1,005.08	498.32
Big Bonds I	110.96	110.96	110.96	110.96	110.96	110.96	110.96	110.96
Big Bonds II	34.55	36.14	39.71	42.57	45.63	48.92	52.45	56.21
Big Bonds III	30.31	32.53	34.93	37.48	40.23	43.17	46.35	49.74
Big Bonds IV	249.81	280.66	153.10	0.00	0.00	0.00	0.00	0.00
JDA Bond	191.58	95.81	0.00	0.00	0.00	0.00	0.00	0.00
JDB Bond	183.36	183.39	0.00	0.00	0.00	0.00	0.00	0.00
BRA Bonds I	86.99	92.26	97.87	103.85	110.17	116.87	124.01	131.53
BRA Bonds II	14.92	15.65	16.44	17.28	18.15	19.08	20.04	21.05
BRA Bonds III	31.42	33.71	36.19	38.84	41.68	44.74	48.02	51.54
BRA Bonds IV	20.81	21.86	22.97	24.13	25.36	26.64	28.00	29.40
BRA Bonds Va	0.00	35.15	37.32	39.57	42.00	44.54	47.27	50.15
BRA Bonds Vb	0.00	114.25	122.36	131.11	140.43	150.45	161.14	172.62
Eurokuna due 98	300.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Interest payments	801.21	808.77	629.58	543.72	465.29	385.34	302.27	217.67
FFED	359.23	309.58	259.93	210.27	160.62	110.97	61.32	11.67
Big Bonds II	55.32	52.83	50.17	47.30	44.24	40.96	37.43	33.65
Big Bonds III	52.74	50.52	48.12	45.56	42.82	39.87	36.70	33.31
Big Bonds IV	74.76	43.87	9.20	0.00	0.00	0.00	0.00	0.00
JDA Bond	60.92	30.48	0.00	0.00	0.00	0.00	0.00	0.00
JDB Bond	39.08	39.08	0.00	0.00	0.00	0.00	0.00	0.00
BRA Bonds I	68.06	62.45	56.84	50.90	44.58	38.37	30.70	23.19
BRA Bonds II	15.21	14.45	13.67	12.84	11.96	11.04	10.07	9.07
BRA Bonds III	54.64	52.35	49.87	47.22	44.37	41.32	38.04	34.52
BRA Bonds IV	21.25	20.19	19.09	17.92	16.70	15.42	14.07	12.66
BRA Bonds Va**	0.00	23.82	21.65	19.41	17.02	14.44	11.71	8.83
BRA Bonds Vb**	0.00	109.16	101.05	92.30	82.98	72.96	62.23	50.79
Eurokuna due 98	37.50	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Debt Service Total:	3,060.99	2,866.24	2,306.52	2,094.58	2,044.99	1,995.79	1,945.59	1,389.19

Source: Ministry of Finance

*Excluding bonds for reconstruction

** Bonds for bank rehabilitation - series Va, Vb are issued according to the Decision on the rehabilitation and restructuring of Dubrovačka banka d.d. Dubrovnik II - description in text

Table 4: Internal debt stock (HRK millions)

Stock (end of year)	1998	1999	2000	2001	2002	2003	2004	2005
<i>FFED</i>	6,424.81	5,523.72	4,518.64	3,513.56	2,508.48	1,503.40	498.32	0.00
<i>Big Bonds I</i>	1,463.41	1,331.54	1,220.58	1,109.62	998.66	887.70	776.73	665.77
<i>Big Bonds II</i>	746.05	719.71	680.00	637.43	591.80	542.88	490.43	434.22
<i>Big Bonds III</i>	736.39	704.19	669.26	631.78	591.54	548.37	502.02	452.28
<i>Big Bonds IV</i>	433.77	153.10	0.00	0.00	0.00	0.00	0.00	0.00
<i>JDA Bond</i>	95.80	0.00	0.00	0.00	0.00	0.00	0.00	0.00
<i>JDB Bond</i>	183.37	0.00	0.00	0.00	0.00	0.00	0.00	0.00
<i>BRA Bonds I</i>	1,064.17	971.91	874.04	770.19	660.02	543.15	419.15	287.62
<i>BRA Bonds II</i>	300.68	285.28	268.84	251.56	233.41	214.33	194.29	173.23
<i>BRA Bonds III</i>	747.33	729.67	693.48	654.64	612.96	568.22	520.20	468.66
<i>BRA Bonds IV</i>	411.59	398.46	375.49	351.36	326.00	299.36	271.36	241.96
<i>BRA Bonds Va</i>	405.68	370.53	333.21	293.64	251.64	207.10	159.83	109.69
<i>BRA Bonds Vb</i>	0.00	1,473.33	1,350.97	1,219.85	1,079.43	928.98	767.84	595.21
<i>Eurokuna due 98</i>	0.00							
TOTAL	13,013.03	12,661.44	10,984.50	9,433.63	7,853.93	6,243.48	4,600.16	3,428.65

Source: Ministry of Finance

*Excluding bonds for reconstruction

Since the State Bank Rehabilitation Agency has assumed the obligations of Dubrovačka banka from the CNB as to the interim financing of liquidity granted to Dubrovačka banka by the CNB in 1998, the early redemption of one part of the issued bonds was executed, so that the debt position in June 1998 was reduced to HRK 501.5 million. After the regular redemption in November the debt position in the DAB-V series at the end of 1998 accounted for HRK 4.405.68 million, as shown in Table 4.

At the beginning of 1999, the new Decision on the Rehabilitation and Restructuring of Dubrovačka banka d.d. Dubrovnik (II)¹⁰ was passed. This passage annulled the provisions of the Decision on the Rehabilitation and Restructuring of Dubrovačka banka d.d. Dubrovnik of April 16 1998.

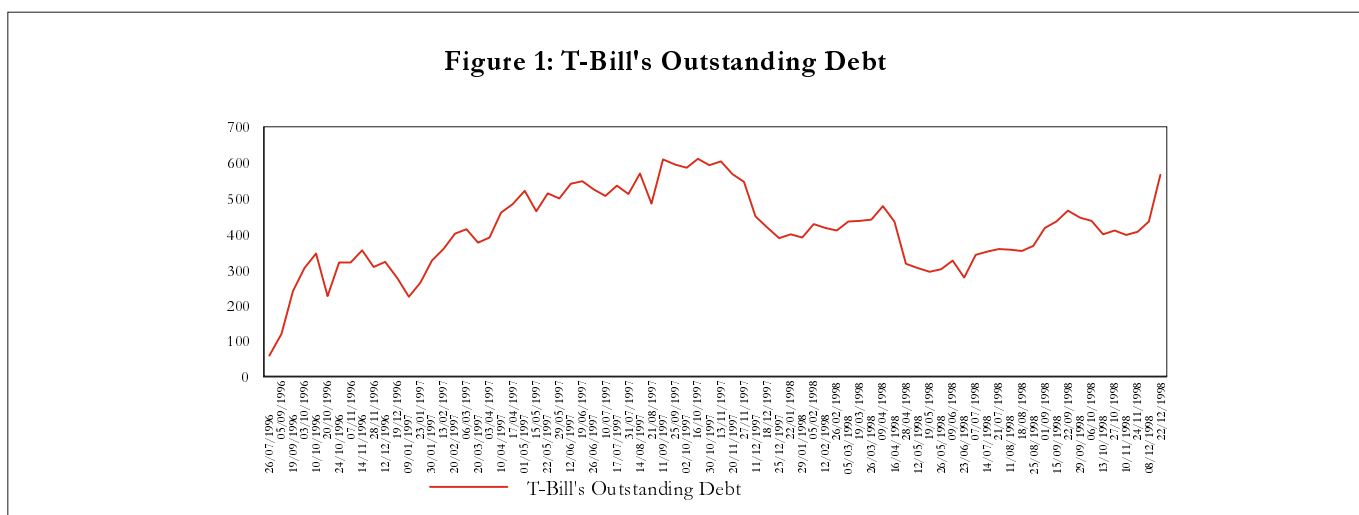
In accordance with the Decision on the Rehabilitation of Dubrovačka banka (II), bonds in the amount of HRK 2,601.8 million were issued. They include an amount of HRK 1,001.5 million, which was the amount of the bonds issued according to the first Decision plus HRK 1,415.3 million for covering potential losses, which could not be charged at the expense of equity capital, plus HRK 185 million for the bank's additional capital investments.

In exchange for unredeemed bonds issued in accordance with the Decision on the Rehabilitation of Dubrovačka banka (I), the DAB-Va bonds with the currency clause, interest rate of 6 percent and 10 year maturity date were issued. The annuity payment of the DAB Vb series will be conducted on May 15 and November 15, under condition that May 15, 1998 is considered the first redemption.

Also, the DAB Vb series bonds were issued in the amount of HRK 1,600.3 million against the currency clause (equivalent value in Euro according to the CNB mean exchange rate on January 28, 1999). The DAB Vb bonds were issued with a 7 percent interest rate and a 10 year maturity date. Annuities will be paid out on May 15 and November 15 so that the first annuity will be due on May 15, 1999.

2.1. TREASURY BILLS

Treasury bills are short-term securities issued by the Finance Ministry. Treasury bills are issued at a unified disposal price realised at an auction. The planned issue amount is determined by the Finance Ministry by an invitation for bids. The collected bids are ranked in accordance with the offered price. When the amount of the bids ranked in such a way reaches the planned issue amount, the Finance Ministry determines the unified disposal price in accordance with the threshold bid, i.e., with the last ranking bid by means of which the planned issue amount has been reached. Offers with a lower price are automatically rejected.

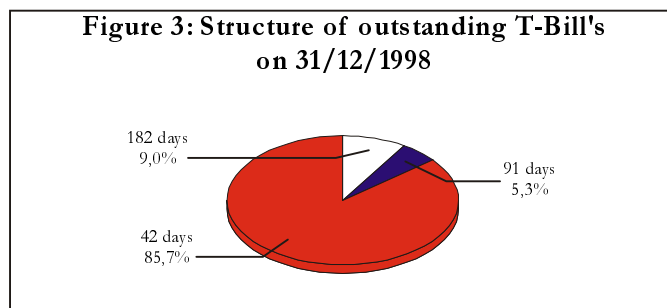
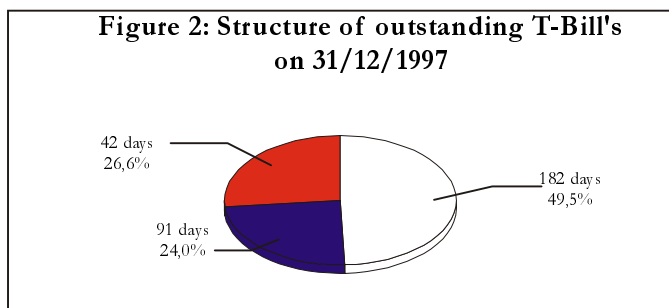


33 treasury bills auctions were conducted during 1998. The total amount of the issued treasury bills on December 31, 1998 accounted for HRK 565.8 million, whereas at the end of 1997 unredeemed bills amounted to HRK 388.1 million. The liability trend in treasury bills is shown in Figure 1.

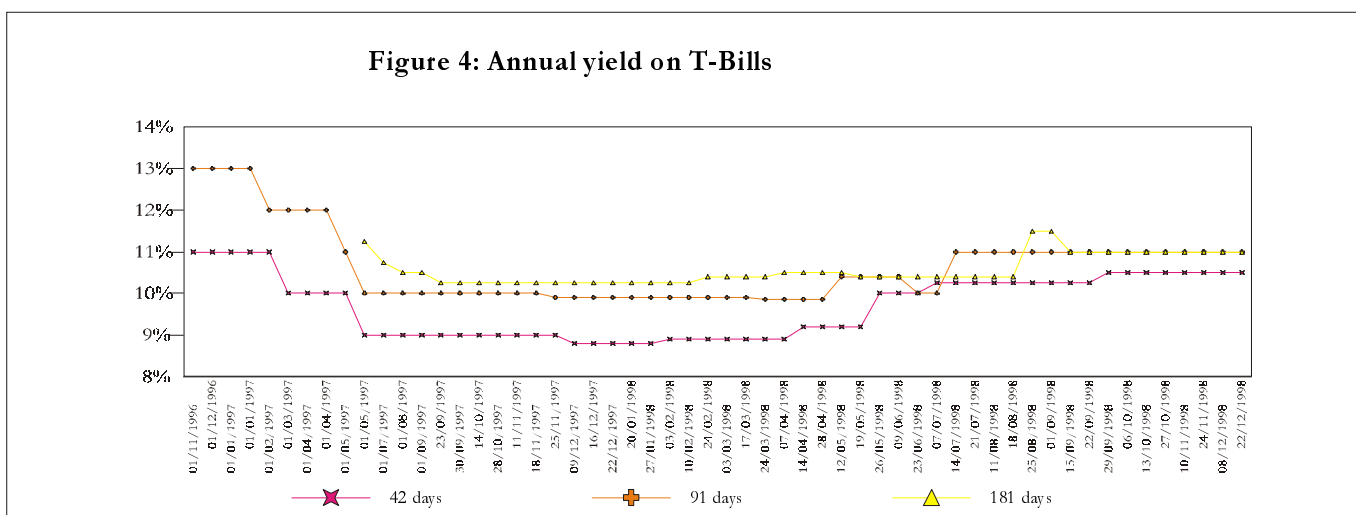
Figure 2 presents the structure of issued treasury bills according to maturity date on December 31, 1997, whereas Figure 3 shows the structure of treasury bills on December 31, 1998. It is evident that during 1998

¹⁰ Decision on the Rehabilitation and Restructuring of Dubrovačka banka d.d. Dubrovnik (II), *Narodne novine* No. 11/99

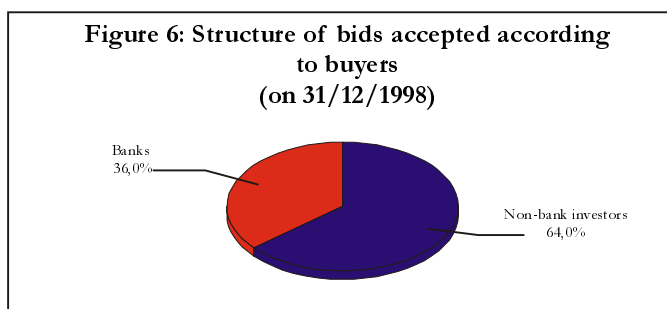
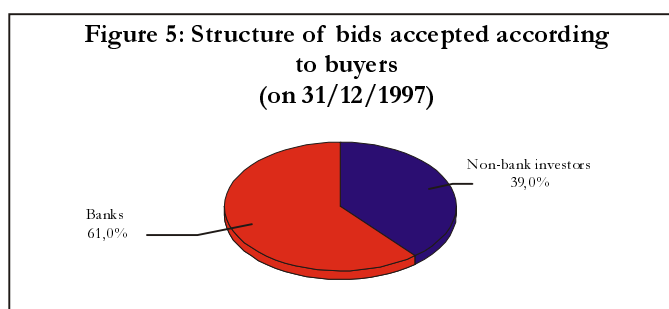
there was a change in the maturity structure as to the treasury bills with a shorter maturity date. Such a change in the maturity date structure is a logical consequence of restrictive policies that were applied in other banks by the CNB, particularly in the second half of the year.



After April interest rates began to rise as well. At auctions held during the three first months in 1998, treasury bills with a 42 days maturity date were issued at an interest (discount) rate of 8.8 percent or 8.9 percent. However, for the same category of treasury bills, the interest rate increased in April to 9.2 percent, reaching 10.6 percent by the end of the year. A similar trend, as shown in Figure 4, was also recorded in interest rates on treasury bills with different maturity dates.



During 1998, the structure of buyers also changed. As shown by Figures 5 and 6, in 1997 the majority of treasury bill buyers were banks, which changed considerably in the course of 1998. Contrary to the situation in 1997, at the end of 1998 the most important treasury bills buyers were not representatives of the banking sector.



3. FOREIGN DEBT OF THE REPUBLIC OF CROATIA

According to the Croatian National Bank data, foreign debt on December 31 1998 amounted to US\$ 3,225.8 million. Debts of the former SFRY, which the Republic of Croatia took over by the London and Paris Club Agreement, amounted to HRK 1,836 million by the end of 1998 and made 57 percent of total foreign public debt.

The methods and conditions for assuming a part of the debt of the former Yugoslavia owed to creditors, members of the Paris and London Clubs, are described in detail in the "Annual Report of the Finance Ministry, 1994-1997".

Features of the bonds issued independently on the international capital market by the Republic of Croatia until December 31 1998 are shown in Table 5.

Table 5: Outline of International Bonds of the Republic of Croatia

<p>Euro-dollar bonds US\$ 300 million - 5 yrs, bullet - 7% coupon (80 bp over 5 year Treasuries) Led by: Merrill Lynch and UBS Signed: February 1997 Listing: Luxembourg</p>	<p>Euro-ATS bond ATS 700 million - 5 yrs, bullet - 5.625% coupon Led by: Creditanstalt Signed: May 1997 Listing: Wien</p>
<p>Euro-DM bond DEM 300 million - 7 yrs, bullet - 6.125% coupon (95bp over relevant Bond) Led by: Credit Suisse and Deutsche Morgan Grenfell Signed: June 1997 Listing: Frankfurt</p>	<p>Matador Bonds -ESP 15 billions - 6.5% coupon Led by : Banco de Santander Signed: March 1998 Listing: Madrid</p>

Source: Ministry of Finance

A review of the repayment system for principal and interest on all bonds (including replacement bonds issued in exchange for acquired debts owed to the London Club) and on commercial bank loans is presented in Table 6. Table 6 also contains a repayment schedule for bonds denominated in Eurasia, which Croatia issued in March this year and which, for this reason, are not included in the Table showing debts at the end of 1998.

A detailed review of the debt position owed to official creditors is given in the following paragraph.

3.1. REPUBLIC OF CROATIA BONDS DENOMINATED IN EUROS

In March 1999, the Republic of Croatia issued Eurobonds denominated in Eurasia in the amount of EUR 300 million, with maturity in 2006 and an annual interest warrant of 7.375 percent, i.e., against a premium of 3.75 percent above the corresponding seven-year German bonds.

The principal co-ordinators of the issue were Credit Suisse, First Boston and Dresdner Klienwort Benson, and a syndicate of fourteen banks monitored the issue. The investor structure according to country is shown in Figure 7.

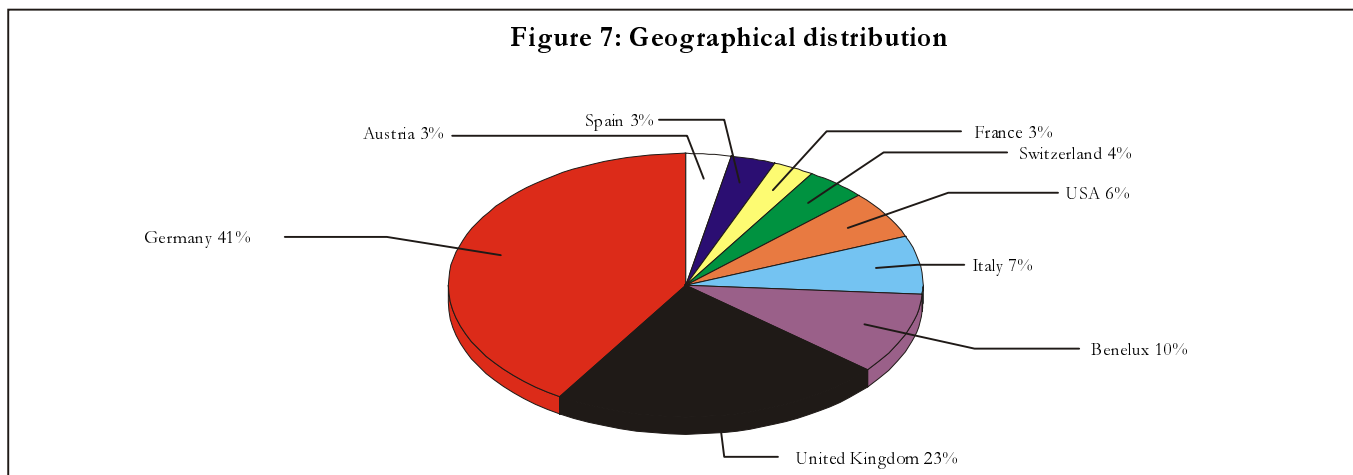


Table 6: International bonds and loans issued or guaranteed by the Republic of Croatia

	Currency	Amount issued	USD*	1997	1998	1999	2000	2001	2002	2003	2004	2005
London Club Series A	USD	857,796,000	857,796,000	0	0	0	77,981,455	77,981,455	77,981,455	77,981,455	77,981,455	77,981,455
- coupon: 6m LB+13/16				57,352,240	57,077,745	52,325,556	51,467,760	50,371,146	45,204,874	40,038,603	34,872,332	29,706,060
London Club Series B	USD	604,426,000	604,426,000	33,777,040	23,777,040	23,777,040	47,554,080	71,331,120	71,331,120	83,219,640	83,219,640	83,219,640
- coupon: 6m LB+13/16				39,698,699	37,583,207	33,359,187	31,908,788	30,323,156	25,597,470	20,674,879	15,161,578	9,648,277
Eurokuna	HRK	300,000,000	48,019,208	0	47,204,695	0						
- coupon: 12.5%				5,689,172	5,900,587	0						
EuroUSD	USD	300,000,000	300,000,000	0	0	0	0	0	300,000,000	0		
- coupon: 7%				10,500,000	21,000,000	21,000,000	21,000,000	21,000,000	10,500,000	0		
EuroDM	DM	300,000,000	179,577,431	0	0	0	0	0	0	0	174,856,481	
- coupon: 6.125 %				0	10,709,959	10,709,959	10,709,959	10,709,959	10,709,959	10,709,959	10,709,959	0
HBOR (guaranteed)	ATS	700,000,000	59,556,975	0	0	0	0	0	58,488,710			
- coupon: 5.625%				0	3,289,990	3,289,990	3,289,990	3,289,990	3,289,990	0		
Matador	ESP	15,000,000,000	103,659,151	0	0	0	0	103,659,151	0			
- coupon: 6.50%				0	0	6,737,845	6,737,845	6,737,845	0			
Dresdner Bank	USD	100,000,000	100,000,000	0	0	0	100,000,000					
- coupon: 6.0%						6,000,000	3,000,000					
Deutsche Bank	DEM	150,000,000	89,788,715	0	0	0	87,428,241					
- coupon: 3mLB+1%						3,594,394	2,888,351					
EURO bond	EURO	300,000,000	330,480,008	0	0	0	0	0	0	0	0	0
- coupon: 7.375%							25,949,788	25,949,788	25,949,788	25,949,788	25,949,788	25,949,788
Total amortization				33,777,040	70,981,735	23,777,040	312,963,776	252,971,726	507,801,285	161,201,095	336,057,576	161,201,095
- London Club				33,777,040	23,777,040	23,777,040	125,535,535	149,312,575	149,312,575	161,201,095	161,201,095	161,201,095
- Bonds				0	47,204,695	0	0	103,659,151	358,488,710	0	174,856,481	0
- Loans				0	0	0	187,428,241	0	0	0	0	0
Total interest payments				113,240,111	135,561,488	137,016,931	156,952,481	148,381,884	121,252,081	97,373,229	86,693,657	65,304,125
- London Club				97,050,939	94,660,952	85,684,743	83,376,548	80,694,302	70,802,344	60,713,482	50,033,910	39,354,337
- Bonds				16,189,172	40,900,536	41,737,794	67,687,582	67,687,582	50,449,737	36,659,747	36,659,747	25,949,788
- Loans				0	0	9,594,394	5,888,351	0	0	0	0	0

Source: Ministry of Finance

* average exchange rate of CNB, end of December, except for EURO bonds where average exchange rate for February was applied

3.2. NEW LOANS ARRANGED WITH THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT IN 1998

Two new loans with a total amount of DM 139,000,000 were arranged with the International Bank for Reconstruction and Development during the course of 1998:

- A loan in the amount of DM 74,000,000.00 raised by the Republic of Croatia on 8 September 1998, as the borrower, to finance the Reconstruction Project for a part of Osijek-Baranja County and Vukovar-Srijem County¹¹. The loan is intended for areas in Eastern Slavonia, Baranja and Western Srijem.
- A loan in the amount of DM 65,000,000.00 raised by the Croatian Bank for Reconstruction and Development (HBOR) on 25 September 1998, with a guarantee from the Republic of Croatia, to finance the Local Infrastructure and Environmental Protection Investment Programme¹².

The stated new loans were agreed upon under standard financial terms, which the IBRD¹³ prescribes for countries of group IV (which includes the Republic of Croatia). The IBRD's financial terms for countries in group IV are: a loan period of 15 years, a 5-year deferral of redemption payments, LIBOR on six-month deposits in German marks increased by a 0.50 percent margin and 0.75 percent annual compensation for unused funds¹⁴. During 1998 there was no withdrawal of funds on the two above-mentioned new loans because these loans did not become effective in 1998.

It should be stressed that the IBRD did not support the Reconstruction Project in the areas of Osijek-Baranja County and Vukovar-Srijem County exclusively by loans, but also through donations. Namely, at the beginning of 1998, the Republic of Croatia requested and obtained a donation (irretrievable funds) in the amount of US\$ 200,000.00 from the IBRD because of the significance of the project and urgency of investment. Those funds were spent to finance a consultant, whose duty was to find optimal solutions in the course of project development (especially concerning the flood protection system) which contributed considerably to the acceleration of preparing all arrangements as to the loan itself. The project was accepted in June, the agreements were signed in September 1998, and the loan became effective at the beginning of 1999¹⁵.

The loan funds for financing the reconstruction project (DM 74 million) are intended for the following:

- reconstruction of the water supply infrastructure with the aim of reducing flood risks, enabling an increase in agricultural production and the reconstruction of the local economy,
- protection of the Kopački rit Nature Park and
- land-mine clearing.

The realisation of the Reconstruction Programme of Eastern Slavonia, Baranja and Western Srijem was entrusted to the company Hrvatske vode (which signed the Project Contract with the IBRD) in co-operation with the State Environmental Protection Administration, the Croatian Mine Clearing Agency and the Interior Ministry. It is expected that the works on the project will be completed by December 31, 2002, under condition that the loan funds may be drawn within 6 years - the latest date for drawing funds being June 30, 2003.

On September 25, 1998, the Republic of Croatia concluded a Guarantee Contract with the IBRD for a loan in the amount of DM 65 million to finance the Local Infrastructure and Environmental Protection Investment Programme. The contract was ratified at the beginning of 1999¹⁶.

¹¹Loan Agreement Confirmation Act between the Republic of Croatia and the International Bank for Reconstruction and Development for the Reconstruction Project for a part of Osijek-Baranja County and Vukovar-Srijem County (Eastern Slavonia, Baranja and Western Srijem) (*Narodne novine-Međunarodni ugovori*, No. 15/1998).

¹²Act on the Confirmation of the Guarantee Contract of the Republic of Croatia for the Local Infrastructure and Environmental Protection Investment Programme between the Republic of Croatia and the International Bank for Reconstruction and Development (*Narodne novine-Međunarodni ugovori*, No. 2/1999).

¹³In accordance with IBRD policy of granting loans to borrowers under conditions tied to the economic strength of member states; the Republic of Croatia belongs to country group IV, which includes member states in which GNP per capita is realised at the level from US\$ 3,036 to 5,295.

¹⁴During the 1998 fiscal year, the IBRD applied a compensation rate on unused loan funds of 0.25 percent annually (according to the decision of the bank's executive directors on the reduction of compensation from 0.75 percent annually to 0.5 percent) and calculated the interest waiver rate at a 0.25 percent rate. During the period from 15.10.1998 to 14.04.1999, the same compensation interest rate of 0.25 percent will be applied, in spite of the 0.75 percent rate, which was agreed upon. However, the interest waiver rate is reduced by 0.20 percent, i.e. the 0.05 percent rate will be applied.

¹⁵The loan became effective on January 6, 1999 after the Loan Agreement Confirmation Act entered into force (24.11.1998) and other legal terms were fulfilled.

¹⁶Act on the Confirmation of the Guarantee Contract of the Republic of Croatia for the Local Infrastructure and Environmental Protection Investment Programme between the Republic of Croatia and the International Bank for Reconstruction and Development (*Narodne novine-Međunarodni ugovori*, No. 2/1999).

It should be mentioned that the IBRD, in co-operation with the EBRD¹⁷, is financing the Local Infrastructure and Environmental Protection Investment Programme, and the aim of the project is the ecological revitalisation of Kaštele Bay. The project solves the problem of wastewater discharge and sea pollution in the area of Kaštele Bay, Trogir Bay, the Split Channel and the Brač Channel in accordance with the ecological standards of the Republic of Croatia and European Union, enhances the reliable and safe drinking water supply and improves operative and financial business activity and management of the company for public utilities, Vodovod i kanalizacija Split. This project's implementation has been entrusted to the agency EKO Kaštelanski zaljev and to the companies KP Vodovod and Kanalizacija Split in co-operation with the company Hrvatske vode, which is in charge of supervision. The loan funds will be used through the HBOR by the cities of Split, Solin, Kaštela and Trogir as well as by the companies KP Vodovod and Kanalizacija Split.

The Republic of Croatia, in accordance with the Guarantee Contract, guarantees that the borrower's (HBOR) obligations will be settled duly and on time and it assumes the obligation of securing irretrievable funds to finance the project in the amount of not less than DM 100.3 million which will be financed out of the state budget (equivalent value of DM 75.84 million in HRK in the period from 1999 to 2002) and through investments made by the company Hrvatske vode (equivalent value of DM 24.48 million in HRK).

3.2.1. The course of negotiations on the arrangement of other loans in 1998

After two years of intensive negotiations and preparations¹⁸, the negotiations with the IBRD on a loan to finance the Railway Modernisation and Reconstruction Project were concluded in November 1998. The loan has an amount of EUR 85.4 million. Texts of the project agreements and the operational planning of the project have been previously agreed, so that the project is supposed to be completed by December 31 2002. The EBRD supported the project through a loan in the amount of US\$ 35 million (concluded on December 8 1998) intended to reconstruct and modernise diesel and electric locomotives.

Co-operation with the IBRD on the preparation of the agreement and other documents for signing continued during December 1998 and it was agreed that all deals will be finished during January 1999¹⁹. The Government of the Republic of Croatia accepted the Privatisation Plan of the activities outside the main domain of Croatian Railways and agreed upon the text of the Development Policy Letter. In the Development Policy Letter, addressed to the IBRD, the policy and the measures of the Government of the Republic of Croatia are outlined and support is given to the entire Croatian Railways Modernisation and Restructuring Programme. The programme includes: priority investments, personnel reductions, regulatory system reform, management improvement and economic and financial restructuring with the aim of improving the financial status of Croatian Railways, and all of this with the aim of transforming Croatian Railways into a commercially sound company.

The preparations for the following projects began in 1998: pension and health system reform, structural adaptation of the public sector, Croatian judiciary modernisation, rehabilitation of the cultural heritage in Kaštele Bay, technical help II, support to small businesses and other projects, which will be financed through IBRD loans in 1999 and subsequent years.

3.2.2. Debts owed to the IBRD

In the period from 1994 to 1998, the Republic of Croatia, as a direct debtor, arranged ten long-term loans with the IBRD to finance different programmes and projects. In the same period Croatian banks raised two loans with government guarantees²⁰. As already explained in the "Annual Report of the Finance Ministry,

¹⁷The European Bank for Reconstruction and Development (EBRD) from London supported the Kaštele Bay rehabilitation project with DM 74.64 million already in 1996 within a loan with a total amount of DM 105 million granted to the HBOR, with the guarantee of the Republic of Croatia for the Local Infrastructure and Environmental Protection Investment Programme (see: Act on the Confirmation of the Guarantee Contract of the Republic of Croatia for the Local Infrastructure and Environmental Protection Investment Programme between the Republic of Croatia and the European Bank for Reconstruction and Development (*Narodne novine-Međunarodni ugovori*, No. 4/1999)).

¹⁸Preparations already began in 1995, when the Republic of Croatia was granted a donation by the IBRD in the amount of JPY 58.8 million for the Croatian Railways Restructuring Project.

¹⁹The Loan Agreement between the Republic of Croatia and the International Bank as well as the Project Agreement between the International Bank for Reconstruction and Development and the Croatian Railways were signed on January 20 1999. The Confirmation Act of the Loan Agreement between the Republic of Croatia and the International Bank for Reconstruction and Development for the project of railway modernisation and restructuring was published in *Narodne novine-Međunarodni ugovori*, No. 4/1999.

²⁰To finance the Investment Recovery Project, a total of DM 52 million was granted to four banks (Varaždinska banka d.d. - DM 13.9 million, Dalmatinska banka d.d. - DM 15.6 million, Slavonska banka d.d. - DM 17.3 million and Alpe Jadran banka d.d. - DM 5.2 million) which raised loans with guarantees from the Republic of Croatia. The HBOR raised loan No. 43520-HR in the amount of DM 65 million for the Local Infrastructure and Environmental Protection Financing Programme.

1994-1997", Croatia, after becoming member of the IBRD, also assumed a part of the debt of the former Yugoslavia. One of them is a loan for the Water Supply Project in Istria, which Croatia assumed as a debtor and from which funds are still being drawn²¹. The review of all aforementioned loan categories and the debt position on December 31, 1998 is shown in Table 7. The total value of all loans, which the Republic of Croatia assumed or arranged with the IBRD, either as a debtor or a guarantor, accounts for US\$ 244.83 million and DM 156.3 million, i.e., US\$ 338.38 million.

In the period from 1995 to 1998, total amounts of US\$ 243.13 million (71.51 percent of the arranged total loan amount in US\$) and DM 156.28 million (30.28 percent of the arranged total loan amount in DM) were utilised. During the 1998 fiscal year, total amounts of US\$ 18.21 million and DM 61.31 million of IBRD loan funds (public and publicly guaranteed) were utilised for the realisation of arranged projects and programmes. The funds were utilised in accordance with arranged utilisation time limits, dynamics of works on projects and financing possibilities through domestic resources.

Unused portions of the loans account for US\$ 96.86 million (28.49 percent of the arranged loan amounts in US\$) and DM 359.81 million (69.72 percent of the arranged loan amounts in DM). Fees are charged against the portions that have not been used and they are determined by the provisions of the IBRD. Non-used portions of the loans will be used to finance programmes and projects within time limits provided by agreements, i.e. within the period from 1999 to 2006.

All mature liabilities on inherited and new loans owed to the IBRD were settled duly and on time. The liabilities on eight public loans were settled directly from the Central Budget. They mostly concerned interest rates and fees for unutilised funds, because the first principal was due on the loan for the Urgent Reconstruction Project. The Croatian Health Insurance Fund settled the liabilities on the loan for the Health System Project. Commercial banks, i.e. borrowers, settled mature interest rates and fees on the loan for the Investment Recovery Project, granted with the guarantee from the Republic of Croatia.

Interest on loans in German marks were paid at an annual rate of 3.90 percent to 4.03 percent, whereas interest on loans in U.S. dollars were paid at rates of 5.86 percent and 5.97 percent for single currency loans, and at 6.54 percent and 6.36 percent for currency basket loans. The amount of applied interest rates also includes a margin of 0.5 percent. Fees for unutilised loan principal are calculated and charged at a rate of 0.25 percent annually.

Since mature liabilities were settled duly and on time and the IBRD's strict financial discipline rule were observed, significant savings have been realised in the period from 01.07.1997 to 30.06.1998 (IBRD FY) as to the interest waiver rates on loans which were utilised by the Republic of Croatia (central budget) and they account for US\$ 528,638.18²².

The rest of the debt on two inherited loans (on loan No. 1066-0HR for water supply construction in Dubrovnik and on loan No. 2338-2HR for the construction of 380 kV-net) was completely serviced during 1998, so that there are six inherited loans left, which were assumed with the guarantee from the Republic of Croatia on the basis of which the total debt on December 31, 1998 accounts for US\$ 18.84 million.

In 1998, inherited loans (except for the railway modernisation loan, on which a fixed interest rate of 7.25 percent is applied, and the water supply construction loan in Dubrovnik, serviced at a fixed interest rate of 8 percent annually) were serviced at a floating rate (VLR) of 6.54 percent in the first half of the year and 6.36 percent in the second half of the year.

Liabilities on the four inherited loans utilised to finance railways, roads and the water supply were settled by funds from the Central Budget for 1998²³ intended for these purposes. Moreover, the Central Budget, on the basis of the guarantee of the Republic of Croatia, settled mature liabilities in cases when end-users could not make payments due to insolvency (for example: Varaždinka d.d. Varaždin and Javno poduzeće Vodovod Dubrovnik).

²¹Upon becoming a member of the IBRD, Croatia assumed 7.6 percent of the non-serviced debts of the former Yugoslavia owed to the IBRD, i.e., 16 loans as a guarantor and one loan (for the Water Supply Project in Istria) as a debtor. By the end of 1998, 11 assumed loans were completely serviced.

²²The IBRD grants reduced interest rate only to those debtors, who fulfil their duties duly and on time (at the latest within 30 calendar days after debt maturity date). During the 1998 fiscal year, the IBRD allowed an interest partial waiver of 0.25 percent annually.

²³The Central Budget of the Republic of Croatia for 1998 and the Central Budget Execution Act of the Republic Croatia for 1998 (*Narodne novine* No. 141/1997).

Table 7: Review of IBRD loan

No.	Name of the project	Signed at:	Currency	Value Agreed	Debt Stock 31/12/1997	Debt Stock 31/12/1998	Not disbursed	Disbursement due	Repayments date	
									First	Last
I. Public loans										
1	Emergency reconstruction loan	27/06/1994	000 USD	128,000.00	119,696.75	123,257.04	4,742.96	31/12/1999	15/12/1998	15/06/2011
2	Health Project	8/03/1995	000 USD	40,000.00	30,208.89	36,156.19	3,843.81	31/12/1999	15/06/2000	15/12/2011
3	Highway Sector Project	27/04/1995	000 USD	80,000.00	58,722.96	58,722.96	21,277.04	31/12/2000	15/12/1999	16/06/2012
4	Capital Market Development Project	23/04/1996	000 DEM	14,200.00	3,969.27	11,926.25	2,273.75	30/06/1999	15/10/2001	15/04/2013
5	Farmer Support Services Project	23/04/1996	000 USD	17,000.00	1,454.34	3,829.99	13,170.01	30/06/2001	01/03/2001	1/09/2012
6	Technical Assistance Project	23/04/1996	000 USD	5,000.00	2,803.97	3,164.63	1,835.37	30/06/1999	15/10/2001	15/04/2013
7	Emergency Transport and Mine Clearing Project	04/12/1996	000 DEM	150,900.00	11,000.00	62,128.84	88,771.16	30/06/2000	15/07/2002	15/01/2012
8	Coastal Forest Reconstruction and Protection Project	31/01/1997	000 USD	42,000.00	0.00	853.49	41,146.51	30/06/2002	15/06/2002	15/12/2013
9	Enterprises and Financial Sector Adjustment Loan	4/06/1997	000 DEM	160,000.00	80,000.00	80,000.00	80,000.00	30/06/1999	15/12/2002	15/06/2012
10	Reconstruction Project for Eastern Slavonia, Baranja and Western Srijem	08/09/1998	000 DEM	74,000.00	0.00	0.00	74,000.00	30/06/2003	15/01/2004	15/07/2013
TOTAL I:			000 USD	312,000.00	212,886.90	225,984.30	86,015.70			
			000 DEM	399,100.00	94,969.27	154,055.09	245,044.91			
II. Publicly Guaranteed Loans										
1	Investment Recovery Project	04/12/1997	000 DEM	52,000.00	0.00	2,230.00	49,770.00	31/12/2001	15/03/2003	15/09/2012
2	Municipal Environmental Infrastructure Project	25/09/1998	000 DEM	65,000.00	0.00	0.00	65,000.00	30/06/2006	15/11/2003	15/05/2013
TOTAL II:			000 DEM	117,000.00	0.00	2,230.00	114,770.00			
III. Inherited Loans										
1	Modernisation of Railways (Fourth Railway Project)	10/07/1974	000 USD	12,274.62	3,367.29	1,158.94	0.00	-	-	01/04/1999
2	Water-Supply and Sewerage (Dubrovnik)	24/12/1974	000 USD	6,000.00	545.32	0.00	0.00	-	-	15/10/1998
3	Third Power Transmission (Construction of 380 kV network)	5/10/1983	000 USD	18,900.00	8.47	0.00	0.00	-	-	1/03/1998
4	First Petroleum Sector Project (Oil and Gas Research)	13/12/1985	000 USD	55,000.00	11,382.08	6,845.28	0.00	-	-	1/05/2000
5	Highway Sector Project (Construction of Roads XII Loan)	27/02/1987	000 USD	33,378.00	9,748.00	6,968.00	0.00	-	-	1/04/2001
6	Second Highway Sector	30/09/1988	000 USD	5,900.00	2,437.10	1,952.04	0.00	-	-	15/09/2001
7	Energy Conservation and Substitution Project	30/09/1988	000 USD	1,303.49	570.27	407.34	0.00	-	-	15/02/2001
8	Istria Water Supply Project	01/02/1990	000 USD	28,000.00	2,231.94	1,509.48	13,890.00	30/06/1999	-	15/04/2004
TOTAL III:			000 USD	160,756.10	30,290.47	18,841.08	13,890.00			
TOTAL (I+II+III)			000 USD	472,756.10	243,177.37	244,825.39	99,905.70			
			000 DEM	516,100.00	94,969.27	156,285.09	359,814.91			
TOTAL*			000 USD		300,025.97	338,377.64				

Source: Ministry of Finance

* according to average exchange rate December 1998

3.2.3. Drawing funds during 1998

US\$ 18.22 million out of loans granted in U.S. dollars and DM 61.32 million out of loans granted in German marks during 1998. These funds were used to finance reconstruction projects as well as other projects.

Altogether six public loans for reconstruction financing were arranged in the period from 1994 to 1998 (together with a new loan for water supply infrastructure reconstruction in eastern Slavonia in the amount of DM 74 million). These are as follows: four loans in U.S. dollars in the amount of US\$ 290 million and two loans in German marks in the amount of DM 224.9 million - an overall total of US\$ 424.6 million.

According to the data with a closing entry on December 31, 1998, the following funds were utilised for the realisation of the reconstruction project in the period from 1994 to 1998:

- US\$ 222.03 million or 76.56 percent of funds granted in the form of loans in US\$, the amount of US\$ 67.97 million is still unutilised
- DM 62.13 million, i.e., 41.17 percent of DM 150.9 million of the loans intended for the reconstruction of roads and mine clearing. For these purposes there are still DM 88.77 million or 58.83 percent of loan funds left, which were granted by the IBRD and intended for the reconstruction of roads and mine clearing. There was no drawing on the loan for water supply reconstruction in Eastern Slavonia (DM 75 million) granted in 1998.

The previously mentioned data on loan utilisation include also utilisation during 1998. However, when only utilisation's during 1998 are taken into account, it is evident that during 1998 the following funds were utilised:

- US\$ 13.4 million or only 6 percent of all unutilised funds of the reconstruction loans in U.S. dollars. These 13.6 million were used for urgent reconstruction projects (US\$ 6.6 million), health system rehabilitation (US\$ 5.94 million) and rehabilitation and protection of forests in the coastal area (US\$ 0.85 million)
- DM 51.12 million or 82.3 percent of all unutilised funds of the loans granted in German marks, which were used for the reconstruction of roads and mine clearing.

Apart from the drawing of funds for reconstruction projects, in 1998 DM 7.95 million was utilised to finance the Capital Market Development Project, US\$ 2.37 million for agriculture development, US\$ 2.07 million for water supply system construction in Istria, DM 2.23 million for private company investment projects. All this was realised through placements by commercial banks.

3.2.4. Donations

Altogether fourteen (14) donations granted by the IBRD were arranged for the preparation and realisation of projects in the period from 1995 to 1998. The review of the obtained donations is shown in Table 8.

The donations were as follows:

- nine donations in U.S. dollars in the total amount of US\$ 3.35 million, out of which over US\$2 million were utilised till 31 December 1998 and
- five donations in Japanese yen in the total amount of JPY 241.6 million, out of which over JPY 217 million were utilised.

Three donations in a total amount of US\$ 1,094,410.00 were granted during 1998, out of which US\$ 754,410 was utilised. Preparations for realisation of two new donation agreements also began during 1998. Their total value should account for US\$ 356,580.00. These two donations, which will be realised during 1999, are intended for:

- Project to Solve the Year 2000 Computer Problem - US\$ 80,000.00
- Environmental Protection and Institutional Development Project - US\$ 276,580.00.

Table 8: Review of obtained donation by IBRD

No.	Signed at:	Project	Currency	Amount	Disbursed	Not disbursed
1.	1995	IDF Grant for Procurement	USD	148,000.00	148,000.00	0.00
2.	1995	Private farmer support	JPY	56,600,000.00	56,600,000.00	0.00
3.	1995	Coastal forest reconstruction and protection	JPY	21,200,000.00	21,100,710.00	99,290.00
4.	1995	Public sector adjustment	JPY	75,600,000.00	75,600,000.00	0.00
5.	1995	Agriculture adjustment	JPY	29,400,000.00	5,303,709.00	24,096,291.00
6.	1995	Croatian railways reconstruction	JPY	58,800,000.00	58,800,000.00	0.00
7.	1996	Infrastructure of city environment	USD	500,000.00	499,563.60	436.40
8.	1996	Transport infrastructure in Zagreb	USD	800,000.00	636,000.00	164,000.00
9.	1997	Strategy of biological	USD	102,000.00	102,000.00	0.00
10.	1997	Private sector development	USD	398,000.00	115,000.00	283,000.00
11.	1997	Public finance management	USD	314,000.00	210,153.71	103,846.29
12.	1998	Eastern Slavonia Emergency Reconstruction Project - Flood Control Component	USD	200,000.00	200,000.00	0.00
13.	1998	Health modernisation	USD	418,260.00	140,000.00	278,260.00
14.	1998	Sava River Flood Protection Project	USD	476,150.00	0.00	476,150.00
TOTAL:			USD	3,356,410.00	2,050,717.31	1,305,692.69
			JPY	241,600,000.00	217,404,419.00	24,195,581.00

Source: Ministry of Finance

3.3. EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT (EBRD)

In accordance with its mandate²⁴ and confirmed business priorities in Croatia, the EBRD continued supporting the development of the private sector during 1998. Such a strategy reflected itself through investments in commercial companies, supporting the privatisation and restructuring of companies and banks as well as strengthening the financial sector by granting long-term loans to commercial banks with the aim of reviving long-term housing and mortgage loans. The bank also supported the environmental programme intended to solve the problem of waste disposal in the City of Zagreb, drawn up according to Croatian environmental protection standards as well as European Union standards.

The EBRD financed six new projects in the Republic of Croatia during 1998. The EBRD granted loans in the amount of HRK 101.8 million without state guarantees in 1998: ECU 56.8 million to Zagrebačka banka for housing loans to citizens and ECU 45 million to finance the commercialisation and privatisation of the waste disposal system in Zagreb. The EBRD also invested ECU 30.90 million in private companies and banks - ECU 25.40 million in Podravka for a Vegeta factory in Koprivnica, ECU 11 million in Slavenska banka and ECU 4.5 million in Bank Austria Creditanstalt Croatia d.d.

With the guarantee of the Republic of Croatia, the EBRD supported the Croatian Railways Modernisation and Restructuring Plan in the amount of US\$ 35 million, intended to finance the Railway Locomotives' Reconstruction Project. The Loan Agreement was signed on December 8, 1998 between Hrvatske željeznice d.o.o. and the EBRD with the guarantee of the Republic of Croatia. The loan was granted with a payback period of 12 years with 3-year deferral of redemption payments and at the LIBOR interest rate, applied on six-month deposits in US\$, increased by a margin of 1 percent. The starting front-end fee accounts for 1 percent of the loan amount, the fee for the unutilised part of the loan amount accounts for 1 percent annually and the loan must be utilised by March 31, 2002.

The loan will be used by Croatian Railways to purchase goods and to pay for services necessary to reconstruct diesel and electric locomotives and to pay for consulting services necessary for the realisation and technical supervision of the project. The project should be completed by November 2001. The loan did not become operative at the end of 1998, so that there were no drawings of funds on the loan or liability servicing according to the Guarantee Contract.

²⁴The EBRD was established and conducts business with a special mandate to finance projects which help and accelerate the transition process toward market economies and the development of private and entrepreneurial initiative in the countries of Central and Eastern Europe, which have chosen to apply the principles of multi-party democracy, pluralism and a market economy.

3.3.1. Loan review

In the period from 1994 to 1998, the EBRD financed a total of 26 projects in Croatia, seven in the public sector and nineteen in the private sector.

Total EBRD investments in the public sector account for US\$ 55 million and DM 332.4 million, i.e., a total of US\$ 254 million. The features of the loans granted to the state or obtained with state guarantees are shown in Table 9.

The Republic of Croatia is a debtor in three loans with a total amount of DM 104.4 million and US\$ 20 million, i.e., US\$ 82.5 million. As a debtor, the Republic of Croatia appears in four loans in the total amount of DM 218 million and US\$ 35 million - altogether US\$ 238.9 million.

According to the standing on December 31, 1998 US\$ 17.2 million and DM 69.25 million - altogether US\$ 58.7 million has been drawn in three public loans in which Croatia is a borrower. US\$ 2.79 million and DM 35.14 million were left unutilised.

All matured liabilities on these public loans are settled duly from the Central Budget²⁵. During 1998, Central Budget funds were not used to settle any payments on granted guarantees because the borrowers, Hrvatska elektroprivreda d.d. Zagreb and the Croatian Bank for Reconstruction and Development, settled their due liabilities on time.

²⁵Payments during 1998 were as follows: 1. on the loan in the amount of US\$ 20 million, intended for air flight system construction US\$ 3,420,912.75 (on principal 2,500,000.00 + on interest rates 892,179.36 + on fees 28,733.39); 2. on a loan in the amount of DM 70.9 million, intended for reconstruction of roads: DM 8,322,799.53 (on principal 5,908.33.20 + on interest rates and expenditures 2,414,466.32) and 3. on the loan in the amount of DM 33.5 million for the wholesale market project: fees for unutilised funds in the amount of DM 135,051.53.

Table 9. EBRD Loans

No.	Project	Signed at:	Currency	Loan amount	Interest rate	Disbursed	Not-disbursed	Final date for disbursement	Repayments date first/last	Debt 31/12/1998
1	2	4	5	6	7	8	9 (6-8)	10	11	12
I. PUBLIC LOANS										
1.	Air Navigation System Project	21/09/1994	USD	20,000,000.00	LIBOR +1%	17,200,991.44	2,799,008.56	31/12/1999	21/09/1996 21/03/2004	10,889,160.45
2.	Highway Reconstruction Project	17/01/1995	DEM	70,900,000.00	LIBOR +1%	68,915,286.32	1,984,713.68	28/02/1999	10/04/1998 10/12/2009	63,006,953.12
3.	Wholesale Markets Project	08/12/1997	DEM	33,500,000.00	fixed 7.44%	340,053.08	33,159,946.92	24/11/2001	24/05/2002 24/11/2011	340,053.08
Total I.			USD	20,000,000.00		17,200,991.44	2,799,008.56			10,889,160.45
			DEM	104,400,000.00		69,255,339.40	35,144,660.60			63,347,006.20
II. PUBLICLY GUARANTEED LOANS										
1.	Electric-Network Reconstruction Project	02/02/1995	DEM	63,000,000.00	LIBOR +1%	55,489,295.19	7,510,704.81	31/03/2000	10/03/1998 10/03/2005	47,089,295.19
2.	Tourism Credit Line	26/06/1996	DEM	50,000,000.00	LIBOR +1%	50,000,000.00	0.00	01/05/1998	23/12/1998 23/12/2002	44,444,000.00
3.	Municipal and Environmental Infrastructure Program	09/12/1996	DEM	105,000,000.00	LIBOR +1%	420,198.00	104,579,802.00	31/03/2001	10/04/2001 10/10/2011	420,198.00
4.	Railway Locomotive Rehabilitation Project	08/12/1998	USD	35,000,000.00	LIBOR +1%	0.00	35,000,000.00	31/03/2002	20/05/2002 20/11/2013	0.00
Total II.			DEM	218,000,000.00		105,909,493.19	112,090,506.81			91,953,493.19
			USD	35,000,000.00		0.00	35,000,000.00			0.00
Total I.+ II.			USD	55,000,000.00		17,200,991.44	37,799,008.56			10,889,160.45
			DEM	322,400,000.00		175,164,832.59	147,235,167.41			155,300,499.39

Source: Ministry of Finance

3.4. COUNCIL OF EUROPE SOCIAL DEVELOPMENT FUND (CEF)

The year 1998 represents a turning point in the development of financial co-operation with the CEF because the first CEF loans for the Republic of Croatia were arranged in 1998. These were loans intended for the reconstruction of Eastern Slavonia. The Fund supported reconstruction projects for schools and health care facilities in the territory of Osijek-Baranja County and Vukovar-Srijem County aimed at realisation of the necessary prerequisites for the return of refugees and displaced persons to their homes, accelerated reintegration and the successful resolution of the humanitarian, social and development problems caused by the war. The projects, which were proposed by the Government of the Republic of Croatia in February 1998, were accepted and supported also by the highest authorities of the Council of Europe. Thus Croatia obtained not only significant financial, but also political support.

Since the Administrative Council of the CEF approved project financing in the Republic of Croatia in March 1998, two basic agreements on long-term loans in a total amount of HRK 240,112,129.00 were arranged in July of the same year.

For the Health System Infrastructure Reconstruction Project in Eastern Slavonia²⁶, the basic agreement in the amount of HRK 172,744,129.00 was arranged. The beneficiary of the loan is the Health Ministry.

For the School Reconstruction Project in Eastern Slavonia²⁷ the basic agreement in the amount HRK 67,368,000.00 was arranged. The beneficiary of the loan is the Reconstruction and Development Ministry.

The Health System Infrastructure Reconstruction Project includes the reconstruction of the primary and secondary preventive health care system: the reconstruction/construction of 18 facilities of primary health care and three hospitals, the construction of 48 apartments for medical staff and purchasing of medical equipment. This project will be implemented as a part of the earlier project of health system reconstruction in Eastern Slavonia. The CEF loan intended to finance health system infrastructure reconstruction will finance 44 percent of expenditures estimated in an amount of HRK 388,800.650. The rest of the necessary funds, i.e. 56 percent or HRK 216,056.521, will be secured from the Central Budget. The works must be completed by the end of 2000.

The total value of the School Reconstruction Project in eastern Slavonia accounts for HRK 134,736,000. The planned works include reparation and/or reconstruction and construction as well as providing equipment and its installation in 33 primary and one secondary school in Eastern Slavonia. The arranged CEF loan will be sufficient to finance 50 percent of this project's expenditures, whereas the rest of the necessary funds will be ensured from the Central Budget. The loan will be utilised during 1999.

The basic agreements granted for the period of ten years at the most, with five-year deferral of redemption payments and at market interest rates (LIBOR) reduced by a Fund subsidy of 0.50 percent annually. The subsidy will be settled via the Fund's Selective Trust Account during redemption. The additional agreement will determine the financial terms for each drawing: currency, duration, interest rate, payment date and other factors. The interest on defaulted payments is set at the one-month LIBOR rate increased by 2.5 percent annually.

There were no drawings of funds on these loans in 1998. However, all preparations for signing additional agreements were executed, according to which the funds for conducted works on the reconstruction of schools and health system infrastructure investments will be reimbursed at the beginning of 1999.

²⁶The Act on the Confirmation of the Basic Agreement on the Loan between the Council of Europe Social Development Fund and the Republic of Croatia for Project 1278 (1998) - Health System Infrastructure Reconstruction in Eastern Slavonia (*Narodne novine-Međunarodni ugovori*, No. 13/1998).

²⁷The Act on the Confirmation of the Basic Agreement on the Loan between the Council of Europe Social Development Fund and the Republic of Croatia for Project 1279 (1998) - School Reconstruction in Eastern Slavonia (*Narodne novine-Međunarodni ugovori*, No. 13/1998).

3.4.1. Redemption of inherited loans and debt owed to the CEF

There is a detailed description of the loans granted by the CEF to the former Yugoslavia and assumed by the Republic of Croatia in the "Annual Report of the Finance Ministry, 1994-1997". In accordance with the Act²⁸ and according to redemption plans, DM 724,595.59 of the matured inherited loans were settled to the CEF during 1998 - DM 686,028.35 on principal and DM 38,567.24 for interest. Commercial banks have also duly serviced mature payments, so that the total debt on the old inherited loans reduced from DM 4.11 million in 1997 to DM 1.9 million according to the data on December 31, 1998. Table 11 contains detailed data on debt owed to the CEF.

The rest of the debt, which was assumed in accordance with the Agreement between the CEF and the Republic of Croatia on July 22 1996, was reduced to DM 164,161.64. During 1998, the debt on five inherited loans had been completely serviced, whereas the remaining twelve loans will be serviced as determined by the arranged schedule - by July 30, 2000.

3.4.2. Financial obligations of the Republic of Croatia to the CEF

Upon becoming the member of the CEF²⁹ (June 24 1997), the Republic of Croatia also accepted the financial terms of membership, which include capital share in the amount of ECU 5,534,000.00, payment of one part of the registered capital in the amount of ECU 611,000.00 and the contribution payment to reserves in the amount of ECU 250,000.00. The payments of one part of the registered capital and contribution to reserves in the total amount of ECU 861,000.00 are due in four annual instalments. In 1998, the second instalment in the amount of ECU 215,250.00 was settled. Moreover, in accordance with Section 39 of the Council of Europe Charter, an amount of FRF 36,613.23 was paid in the form of contributions to the budget of the Council of Europe on behalf of CEF business expenditures.

Table 10: The structure of the Republic of Croatia share in the CEF shareholders capital

Repayments		in ECU				
		Called capital (Paid in capital)	Uncalled capital	Subscribed capital	Contribution to the reserves	Total payment obligation
		1	2	3 (1+2)	4	(1+4)
		611,000.00	4,923,000.00	5,534,000.00	250,000.00	861,000.00
Tranches	Date					
I	24/07/1997	152,750.00			62,500.00	215,250.00
II	24/07/1998	152,750.00			62,500.00	215,250.00
III	24/07/1999	152,750.00			62,500.00	215,250.00
IV	24/07/2000	152,750.00			62,500.00	215,250.00

Source: Ministry of Finance

²⁸The Act on the Confirmation of the Basic Agreement on the Loan between the Council of Europe Social Development Fund and the Republic of Croatia, of the Loan Agreement between the Social Development Fund of the Council of Europe and the Republic of Croatia and the Loan Agreements between the Social Development Fund of the Council of Europe and Dalmatinska banka, Privredna banka, Riječka banka, Slavonska banka, Splitska banka and Zagrebačka banka, arranged with guarantees from the Republic of Croatia (*Narodne novine-Međunarodni ugovori* No. 3/1997)

²⁹Act on the Accession of the Republic of Croatia to the Social Development Fund of the Council of Europe and on the Confirmation of the Charter of the Social Development Fund of the Council of Europe as of June 8 1993 (*Narodne novine-Međunarodni ugovori* No. 8/1997)

Table 11: Inherited CEF Loans and Debt Stock

	Final User	Original loan amount (000 DEM)	Tranche	Banks - original debtors	Arrears taken over (000 DEM)			Debt taken over	Debt Stock 31/12/1997	Debt Stock 31/12/1998	Last repayments
					Interest	Principal	Total				
1	Čaraparija, Čakovec	1,011.43	B	Republic of Croatia	123.39	449.52	572.92	224.76	112.38	0.00	14/04/1998
2	Velebit, Karlovac	1,311.38	B	Republic of Croatia	159.99	582.84	742.82	291.42	145.71	0.00	14/04/1998
3	Pamučna predionica, Glina	2,373.99	B	Republic of Croatia	345.94	1,318.89	1,664.83	527.55	236.78	0.00	14/04/1998
4	Agrodelta, Ploče	1,477.46	C	Republic of Croatia	317.16	656.65	973.81	656.65	328.32	164.16	20/08/1999
	Total (1-4):	6,174.26			946.49	3,007.89	3,954.38	1,700.38	823.19	164.16	
5	Vlado Bagat, Zadar	1,927.31	B	Dalmatinska banka, Zadar	280.85	1,070.73	1,351.58	428.29	214.15	0.00	14/04/1998
6	Zdenka (1), V. Zdenci	577.79	C	Privredna banka, Zagreb	0.00	0.00	0.00	256.79	128.40	181.98	20/08/1999
7	Ličanka, Srb	1,548.32	C	Privredna banka, Zagreb	0.00	0.00	0.00	688.14	344.07	172.04	20/08/1999
8	RIZ, Slunj	1,949.96	D	Privredna banka, Zagreb	0.00	0.00	0.00	1,083.31	649.99	433.32	30/07/2000
9	Zdenka (2), Veliki Zdenci	818.90	D	Privredna banka, Zagreb	0.00	0.00	0.00	454.94	272.97	64.20	30/07/2000
10	Torpedo, Rijeka	3,007.08	A	Riječka banka, Rijeka	358.31	1,656.64	2,014.95	334.12	0.00	0.00	12/02/1997
11	Opeka, Đakovo	1,462.84	C	Slavonska banka, Osijek	0.00	0.00	0.00	650.15	325.08	162.54	20/08/1999
12	Tmovača, Sinj	1,133.49	D	Splitska banka, Split	378.62	503.77	882.39	629.71	377.83	251.89	30/07/2000
13	Kordun (1), Karlovac	1,190.00	B	Zagrebačka banka, Zagreb	0.00	0.00	0.00	264.44	132.22	0.00	14/04/1998
14	Kordun (2), Karlovac	1,019.55	C	Zagrebačka banka, Zagreb	0.00	0.00	0.00	453.13	226.57	113.28	20/08/1999
15	Bor, Novi Marof	942.86	C	Zagrebačka banka, Zagreb	0.00	0.00	0.00	419.05	209.52	104.76	20/08/1999
16	Suvremena žena, Zagreb	451.99	C	Zagrebačka banka, Zagreb	0.00	0.00	0.00	200.88	100.44	50.22	20/08/1999
17	Virovitičanka (1), Virovitica	586.09	D	Zagrebačka banka, Zagreb	0.00	0.00	0.00	325.61	195.36	130.24	30/07/2000
18	Virovitičanka (2), Virovitica	350.00	D	Zagrebačka banka, Zagreb	0.00	0.00	0.00	194.44	116.67	77.78	30/07/2000
	Total (5-18):	16,966.17			1,017.78	3,231.14	4,248.92	6,383.03	3,293.25	1,742.25	
	TOTAL (1-18)	23,140.43			1,964.27	6,239.03	8,203.30	8,083.41	4,116.45	1,906.41	

Source: Ministry of Finance

3.5. EUROPEAN INVESTMENT BANK (EIB)

The debt of the Republic of Croatia owed to the European Investment Bank is the result, as described in the "Annual Report of the Finance Ministry, 1994-1997", of the assumption of a part of the debt of the former Yugoslavia³⁰. A review of the inherited loans granted by the EIB, the amount of the inherited debt and the debt position at the end of 1998 is shown in Table 12.

Mature liabilities due to the Luxembourg-based European Investment Bank on the loans utilised for road and railway financing were settled using Central Budget funds³¹, whereas the national electric company Hrvatska elektroprivreda settled its liabilities on loan No. 16275 in the amount of ECU 10.55 million with its own funds. After redemption of all maturity dates in 1998, the debt due to the EIB, expressed in eleven different currencies, accounted for HRK 697,461,725.77 according to the medium exchange rate of the National Bank of Croatia on December 31, 1998.

Table 12: EIB Loans and Debt Stock at the end of 1997

	EIB Loan Mark	New Debtors According to Notes	Guarantee by Notes	Original Loan Value (mill. of ECU)	Currency (in 000)	Debt Stock 31/12/1994	Debt Stock 30/11/1997	Debt 31/12/1998
1	16275 EEMS-HE CRO	HEP d.d. Zagreb Note No. 0297	Republic of Croatia	10,552.00	GRD ITL GBP	161,061.18 4,557,897.06 2,165.21	106,572.52 3,015,913.47 1,432.69	84,087,683.00 2,379,611,306.00 1,130,422.06
2	16279 TYH-II-HC CRO	Republic of Croatia Note No. 0298		16,000.00	GRD DEM USD	372,982.50 4,986.11 7,114.22	284,379.19 3,801.64 5,424.21	248,239,020.00 3,318,510.75 4,734,877.16
3	16284 TYR-I-HZ CRO	Croatian Railways Note No. 0296	Republic of Croatia	19,190.00	FRF DEM DKK USD GBP GRD	33,619.19 17,234.25 33,020.15 2,537.38 904.83 105,884.98	26,336.42 13,500.87 25,867.15 1,987.72 708.82 82,947.61	11,971,537.55 23,353,115.86 628,529.55 22,937,006.42 73,551,579.00 1,762,556.27
4	16289 TYH-III-HC CRO	Republic of Croatia Note No. 0298		15,250.00	DEM FRF GBP ITL DKK USD CHF	834.61 18,025.37 2,141.73 3,058,367.53 12,891.07 2,946.91 514.94	664.63 14,354.28 1,705.54 2,435,492.04 10,265.64 2,346.73 410.07	595,593.20 12,863,239.10 1,528,381.38 2,182,507,604.00 9,199,306.03 2,102,969.41 367,471.88
5	13554 TYH-IV-HC CRO	Republic of Croatia Note No. 0298		60,000.00	GBP NLG JPY BEF DEM CHF	1,798.92 18,891.26 2,977,805.50 164,250.78 15,933.32 18,029.38	1,554.83 16,327.94 2,673,752.10 141,963.86 13,771.36 15,583.00	14,637,042.84 12,935,373.11 15,336,757.42 133,346,032.00 1,460,440.36 2,417,513,988.00
6	14090 TYR-IIB-HZ CRO	Croatian Railways Note No. 0296	Republic of Croatia	18,000.00	DEM CHF USD FRF GBP	9,934.92 6,597.52 2,390.32 27,292.29 2,322.80	8,707.34 5,782.32 2,094.96 23,919.99 2,035.79	8,228,036.08 22,603,293.91 1,923,727.04 5,464,025.84 1,979,643.09
	TOTAL			148,992.00	USD GRD ITL GBP DEM FRF DKK CHF NLG BEF JPY HRK	14,988.82 639,928.66 7,616,264.59 9,333.49 48,923.21 78,936.85 45,911.22 25,141.84 18,891.26 164,250.78 2,977,805.50 877,147.67	11,853.62 473,899.32 5,451,405.51 7,437.67 40,445.84 64,610.68 36,132.79 21,775.39 16,327.94 141,963.86 2,673,752.10 726,815.82	10,580.05 405,878.28 4,562,118.91 6,671.50 37,049.05 58,819.65 32,136.31 20,468.54 15,336.76 133,346.03 2,417,513.99 697,461.73

Source: Ministry of Finance

³⁰Act on the Confirmation of the Guarantee Contract between the Republic of Croatia and the European Investment Bank and of Contract Letter No. 0298 signed on January 12, 1995 in Luxembourg and on February 10 in Zagreb (*Narodne novine-Međunarodni ugovori*, No. 6/1995).

³¹The Central Budget for 1998 and the Act on Calculating the Central Budget of the Republic of Croatia for 1998 (*Narodne novine*, No. 141/1997)

IV. FINANCING OF LOCAL SELF-GOVERNMENT AND ADMINISTRATION UNITS

The Constitution of the Republic of Croatia guarantees citizens the right to local self-government. Pursuant to this right, citizens may decide on their local needs and interests, particularly in the fields of physical planning, urban development, housing, utility services, child care, social welfare, culture, physical culture, sports and environmental protection.

Pursuant to the Local self-government and Administration Act, local self-government units may be municipalities and towns, while counties are self-government and administration units. This Act and other specific legislation regulate the scope of self-government for individual levels of local self-government and administration. The territories of self-government units are determined by law, after the opinion of the respective local population is obtained by means of a survey.

A county is a unit of local self-government and administration whose territory is defined by law. The criteria for the establishment of a county include historical, transit and economic factors, as well as their adequacy for presenting a natural self-government entity within the Republic of Croatia.

Citizens participate directly in the management of local activities within a local self-government unit. The bodies of local self-government units are independent in exercising local activities, and, in accordance with the law and their charters, are accountable for the legality of their actions only to authorised state bodies. In order to exercise state administrative tasks, the bodies of local administration may be established in municipalities or cities, while the specific state administrative activities may be transferred to the jurisdiction of other local self-government units.

The basic task of a local unit is to improve the living conditions of all of its citizens, find ways to achieve economic interests and goals, invest in the utility infrastructure and utility standards and in programs aimed at fulfilling these needs. A county, within the sphere of its self-government jurisdiction, harmonises interests and undertakes activities for the uniform economic and social development of municipalities and cities within its territory, and of the county as a whole.

The County, City and Municipal Territories Act of the Republic of Croatia of 1997 significantly altered the territorial organisation of local units. The previous 425 municipalities were reduced to 429, while the number of cities increased from 75 to 122. The Act established the number of counties at 20, while the City of Zagreb obtained the status of both a city and a county.

1. SOURCES OF FINANCING FOR LOCAL SELF-GOVERNMENT AND ADMINISTRATION UNITS

Local self-government units freely dispose of their revenues within the scope of their self-government jurisdiction. They provide funds for their activities from their own budgets. The Budget Act³² determines their content and budget planning, preparation, passage and the execution of the budgets of local self-government and administration units.

The budget of a local self-government and administration unit is an estimate of annual revenues and income and the established sum of expenditures approved by the representative body of the local unit. The budget shows all revenues and income to which the local self-government unit is entitled, as well as all expenditures for activities within the scope of their self-government jurisdiction.

Based on the guidelines of the Ministry of Finance and on estimates, county governments provide the guidelines for the preparation of the budgets of local self-government units within their territory. The draft budget is prepared by the executive authorities of the local self-government and administration unit at the request of budget users and in compliance with the funds available. The budget is passed for one fiscal year. If the budget is not passed prior to the beginning of the fiscal year, funding is provisional and executed for not longer than three months of the fiscal year. The decision on provisional funding is passed by the representative body of the local self-government unit. Unless the budget is passed by the end of the first quarter of the year, the Government of the Republic of Croatia then dissolves the representative body and instead appoints government commissioner.

All revenues and income must be distributed within the budget and expressed in terms of their sources. Budget expenditures must be determined by the budget and balanced with revenues and income. The general

³² The Budget Act, *Narodne novine* /Official Gazette of the Republic of Croatia/, No. 92/94

section of the budget comprises the revenues and expenditures account and the financing account, while the specific section contains a schedule of expenditures classified by accountable bodies, beneficiaries and purposes. Budget beneficiaries may use budgetary funds only for budget-stipulated purposes and in the amount determined in its specific section. By way of derogation, within the beneficiary's framework of budgetary funds, the reallocation of funds is permitted between individual expenditure items only if so approved.

The Local self-government and Administration Unit Financing Act³³ determines the sources of funding for activities within the scope of self-governing jurisdiction of counties, municipalities and cities. Local self-government and administration units acquire their budgetary funds from their own sources (tax and non-tax), joint revenues (tax and non-tax), and grants (from state and county budgets), in compliance with predetermined criteria. Also, in accordance with the Unit Budget Act, the realisation of capital projects may be funded by borrowing income, as stipulated by law. In compliance with the Central budget Implementation Act and with instructions from the finance minister, local self-government and administration units may conclude loan agreements on both domestic and foreign capital markets, exclusively for funding reconstruction and development programs and projects.

The fundamental characteristic of funding sources of local units is the legally determined distribution of joint tax and non-tax revenues between the state and lower government levels. Joint tax revenues are the income tax, profit tax, gaming tax and property sales tax, and they are distributed between the State, county, city or municipality in the following manner.

In income tax distribution, 70 percent is paid to the central budget, 5 percent to the respective county budget, and 25 percent to the city/municipality in which the taxpayer resides. The distribution is different in the City of Zagreb, since the City of Zagreb has the city and county status. Thus, the City of Zagreb participates with 45 percent in the income tax, paid by taxpayers residing in its territory, while the remaining 55 percent are paid to the central budget.

The profit tax is distributed among the central budget and the county, city and municipal budgets in the following ratios: central budget 70 percent, county 10 percent and city/municipality 20 percent of the profit tax.

The gaming tax is distributed between the central budget, in which 50 percent of the taxes are collected, and cities and municipalities in which the remaining 50 percent are collected.

40 percent of the property sales tax is distributed to the central budget, while 60 percent goes to the city/municipal budgets.

The sources of revenues of counties are:

- County taxes (inheritance and gift tax, motor vehicle tax, seafaring and freshwater vessel tax, entertainment and sporting events tax),
- Monetary fines and seized earnings from illegal activities, as determined by the counties themselves,
- Income from their own assets,
- Other income as stipulated by special legislation.

The sources of revenues of municipalities and cities are:

- Municipal and urban taxes (consumption tax, vacation home tax, advertisement tax, corporate title tax, public land use tax),
- Income from their own assets,
- Monetary fines and seized earnings from illegal activities, as determined by the counties,
- Administrative fees in accordance with special legislation,
- Residence fees in accordance with special legislation,
- Utility charges and contributions and other charges established by special legislation,
- Charges for the use of public municipal or urban lands,
- Other revenues established by special legislation.

According to the Local self-government and Administration Unit Financing Act, cities with 40,000 or more residents may introduce an income surtax (on top of the state income tax) on a portion of the income tax that they are entitled to according to the provisions of the said Act. The income surtax rate may not exceed 30

³³ The Local self-government and Administration Unit Financing Act, *Narodne novine* No. 117/93

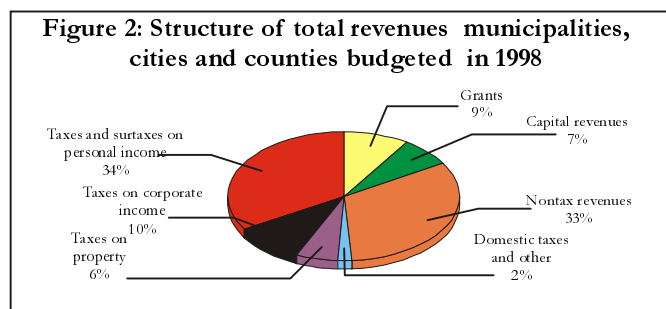
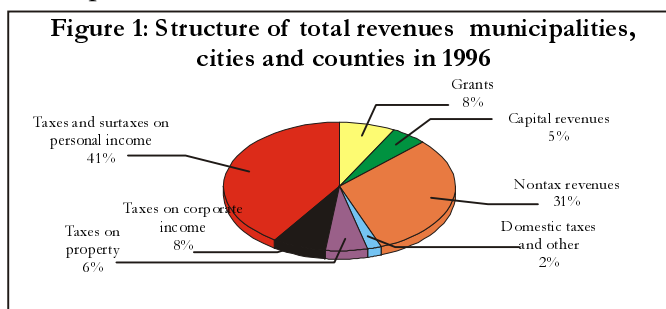
percent (coefficient 1.30). By way of derogation from the provisions of this Act, the City of Zagreb may stipulate an income surtax rate of up to 60 percent (coefficient 1.6). The income surtax is the revenue of the local self-government and administration unit in which the surtax payer resides. The importance of the income surtax in total revenues is easily discernible in the 1997 data showing that 19.61 percent of Zagreb tax revenues, or HRK 370 million, were covered by the income surtax, and in 1998 19.05 percent or HRK 441 million.

The Tax Administration Act provides that the assessment, control and collection of joint tax revenues and county taxes are under the jurisdiction of the Tax Administration. Record keeping, collection and control of revenues for local self-government units are under control of the Tax Administration only on the basis of specific agreements with the local units. If no such agreement has been concluded with the Tax Administration, tax assessment and collection is handled by the local self-government unit independently.

2. REVENUES TRENDS IN LOCAL SELF-GOVERNMENT AND ADMINISTRATION UNITS FROM 1996-1998

The following shows trends in the budget revenues of counties, cities and municipalities in the period from 1996 until 1998. As shown in Figures 1, 2 and 3, taxes are undoubtedly the strongest revenue item in the budgets of local self-government and administration units. However, due to changes in utility services funding and reductions in the tax burdens on income, their significance diminished to the benefit of non-tax revenues. Thus, the share of tax revenues in the structure of total revenues was 56 percent in 1996, 53 percent in 1997, and estimated at 51 percent for 1998. Simultaneously, the share of non-tax revenues in the structure of total revenues grew from 31 percent in 1996 to 33 percent in the 1998 estimates.

The structure of total revenues showed a year-on-year increase in the share of capital revenues - they ranged from 5 percent in 1996 to 7 percent in 1998. The share of grants also showed a slight increase - from 8 percent of total revenues in 1996 to 9 percent of the total budget revenues of counties, cities and municipalities in 1998.



The majority of the tax revenues of local self-government and administration was collected from joint taxes (income and profit taxes), making up 40 percent of its total revenues. It is important to note that the income surtax is included here within the joint income tax, although the first is the original, that is the exclusive revenue of cities. However, due to displaying and monitoring methodology, some self-government and administration units cannot show the income tax separately.

During the period under observation, it is simple to discern the decline in the share of the income tax and income surtax. The decline in importance of this type of revenue was the result of changes in income taxation, which were directed toward a decrease in the income tax rate and an increase in the non-tax portions of income. In 1996, the share of the income tax and surtax made up 72 percent of total tax revenues, while in 1998 it fell to 66 percent.

The decline of importance of the income tax and surtax was accompanied by the continuous growth of the profit tax share in the total revenues of the county, city and municipal budgets: from 7.56 percent in 1996 to 9.49 percent in 1997, while the 1998 estimates expect a 9.61 percent share in total revenues. This growth can be explained by the larger taxation rate, which was increased from 25 percent to 35 percent in 1998, as well as by the enhanced financial discipline of taxpayers. The share of the profit tax in the total revenues also increased from 14 percent in 1996 to 19 percent in 1998.

The described trends, observed in the entire local self-government and administration system, were also discernible in the total revenues of municipalities. The structure of total revenues of municipalities is displayed in Figures 3 and 4. The share of total tax revenues in total revenues in 1996 was 40 percent and in 1998 it fell to 28 percent. The share of non-tax revenues in total revenues grew from 39 percent in 1996 to 41

Figure 3: Structure of total revenue municipalities in 1996

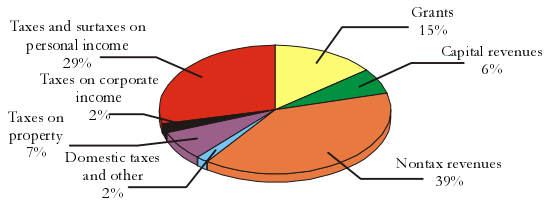
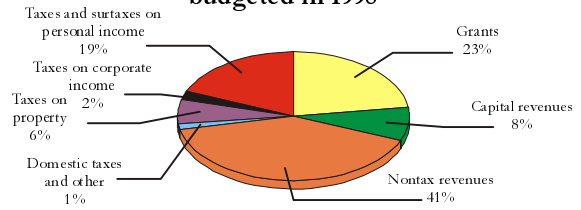


Figure 4: Structure of total revenue municipalities budgeted in 1998



percent in 1997 and 1998. Both, the share of capital revenues and that of grants, tended to increase as well. The share of grants in total revenues in 1996 was 15 percent, 18 percent in 1997, while the 1998 budget showed as much as 23 percent share.

Individual levels of local self-government and administration, when analysed separately, showed different shares of different taxes in their budgets. This comes as a result, as described above, of different methods by which joint taxes were distributed as well as different bases on which taxation rates were applied. However, all levels of local self-government and administration show that local taxes have little importance and, moreover, become less and less significant.

As shown in Figures 5 and 6, the structure of city revenues also show that the importance of tax revenues has decreased to the benefit of non-tax revenues. Grants in city budgets were slightly less significant than in the budgets of municipalities. In 1996, grants made up 2 percent of total revenues and their share grew to 4 percent in 1998.

Figure 5: Structure of total revenues cities in 1996

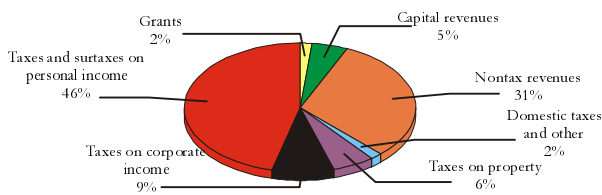
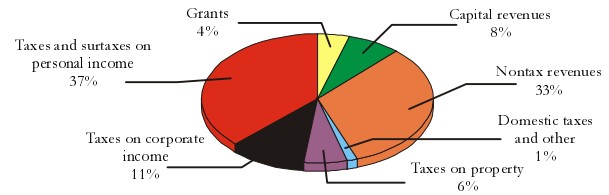


Figure 6: Structure of total revenues cities budgeted in 1998



Tax revenues, as seen in Figures 7 and 8, dominated in the structure of county budgets as well. However, in contrast to the budgets of municipalities and counties, where tax revenues showed downward trends, the share of tax revenues grew in counties. In 1996, their share in total revenues accounted for 45 percent and grew to 53 percent in the 1998 budget. In addition to tax revenues, grants were still important in the structure of county revenues. However, as the Figures show, their significance decreased in comparison to 1996, when their share constituted 33 percent of total revenues, while making up only 25 percent of total revenues in county budgets in the 1998 fiscal year.

Figure 7: Structure of total revenues counties in 1996

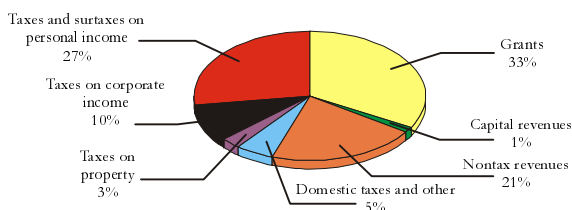
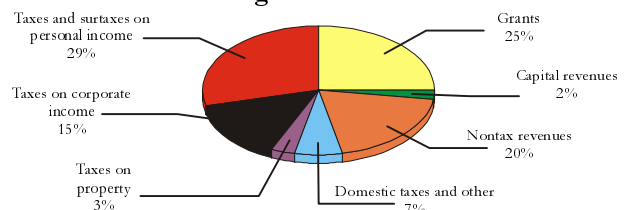


Figure 8: Structure of total revenues counties budgeted in 1998



3. NON-TAX AND CAPITAL REVENUES OF MUNICIPALITIES, CITIES AND COUNTIES

Non-tax revenues (see above Figures 1-8) showed continuous growth in the budgets of cities, municipalities and counties.

The reason why the share of non-tax revenues grew in the total revenues of local self-government and administration was the Utility Management Act, which abolished utility funds, while utility charges and contributions became part of the non-tax revenues of municipal and urban budgets. This growth was also due to higher utility and administrative fees. Thus, their share in total non-tax revenues increased from 12.85 percent in 1996 to 15.12 percent in 1998. However, it should be stressed that these were earmarked revenues, which could only be utilised for the expenditures of utility services.

In compliance with specific legislation, counties, cities and municipalities are entitled to charges and fees which are collected on the basis of this legislation, and which are contained in the non-tax revenues of their budgets. These are charges and fees relating to utility management, utilisation of the sea, mineral rights, use of electrical power plants, public land use, hunting fees, residence fees, stamp duties, etc.

In the non-tax revenues of the budgets of counties, cities and municipalities, administrative fees were the most represented with 66 percent, followed by business income and real estate income with 18 percent and other non-tax revenues with a 16 percent share. As to administrative fees, the most significant share was that of utility charges and contributions as well as the share of joint revenues collected from stamp duties.

Capital revenues were of relatively little importance to local self-government and administration. Capital revenues include revenues from the sale of socially owned apartments, from the sale of state-owned agricultural land as well as revenues from the sale of mobile assets and real estate owned by local self-government and administration units.

The Local self-government and Administration Unit Financing Act established criteria for the allocation of grants from the central budget to the counties. However, in practice these grants were realised in a manner that ensured subsidies to counties but also to municipalities and cities under special state care, in accordance with the central budget's possibilities.

Also, the central budget finances many capital projects at the local self-government level which are not within the scope of mandatory funding from the central budget. Counties as well, within the scope of their possibilities, provide grants and aid to municipalities and cities in their territories, either directly or by co-funding capital and current expenditures. For projects of special state interest, the central government may approve earmarked grants or aid to local self-government and administration units for such municipalities and cities that suffered wartime damages, or it may approve aid that depends on the significance of those units and on the significance of the objective in question.

In 1997, cities, municipalities and counties were allocated transfers from the central budget in the amount of HRK 279,190,600. In 1998, transfers amounted to as much as HRK 493,282,132 or 77 percent above their 1997 levels, and included, besides counties, 23 cities and 57 municipalities in regions under special state care.

4. BUDGET EXPENDITURES OF LOCAL SELF-GOVERNMENT AND ADMINISTRATION UNITS

The structure of municipal, city and county expenditures is presented in the Figures 9 and 10. They show that current expenditures constituted approximately 75 percent of the total expenditures of cities, municipalities and counties, while the remaining portion were capital expenditures and net borrowings.

When observed separately, individual levels of local self-government and administration showed an exceptionally large share of current expenditures in the total expenditures of the city budgets. In 1997, the share of current expenditures in municipal budgets was 59.22 percent, in city budgets 77.87 percent, and in county budgets 75.27 percent. Simultaneously, the growth rate of planned capital expenditures for 1998 of 42.3 percent shows that the investment role of local self-government and administration units was increasing. Such growth of capital expenditures was also possible due to the fact that the central government of the Republic of Croatia issued more borrowing approvals, primarily for the purpose of funding the reconstruction and development of the utility infrastructure.

Figure 9: Structure of total expenditure municipalities, cities and counties in 1996

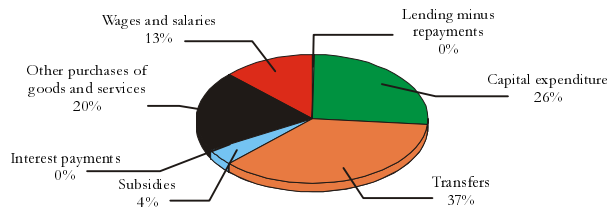
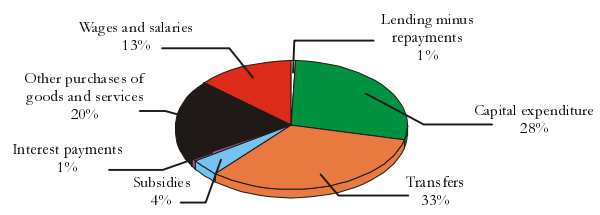


Figure 10: Structure of total expenditure municipalities, cities and counties budgeted in 1998



Current expenditures (expenditures for employees, mandatory contributions for salaries, expenditures for supplies, energy, utilities and other services) are all itemised in county, city and municipal budgets, for employees and officials, as stipulated by respective competent bodies. There are no legally defined limitations on the wage rates of employees but there are limitations for the salaries of officials and contribution rates. In 1997, current expenditures grew by 16 percent, while the revenue growth rate was 14 percent. The 1998 budget estimated the growth of this type of expenditure at a rate of 10 percent, identical to the revenue growth estimates.

Figure 11: Structure of public expenditure municipalities, cities and counties in 1996

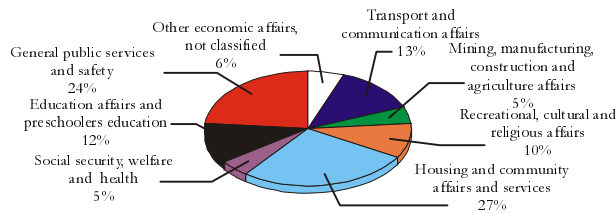
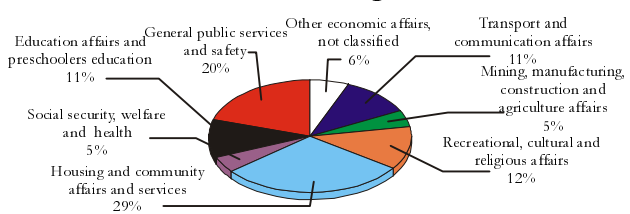


Figure 12: Structure of public expenditure municipalities, cities and counties budgeted in 1998



The majority of current expenditures were subsidies and other current transfers, which made up 41.2 percent of total 1997 expenditures, or 16 percent in excess of the amount spent in the previous year. The largest portion of transfers of local self-government and administration units were transfers to non-profit institutions and associations such as kindergartens, theatres, technical culture, sports and utility companies. Transfers and subsidies included programs and activities but also salaries and material costs, which should be listed within expenditures for goods and services.

If local levels are observed in terms of function, it can be seen that the largest portion was occupied by functions of general public services and housing and utility management. Figures 11 and 12 show the share of individual functions in the total expenditures of cities, municipalities and counties.

Table 1: Functional classification of expenditure by Function municipalities, cities and counties in 1996-1998

	1996	1997	Plan 1998
Total expenditure by function	6,489,636,141	7,414,763,060	9,127,238,595
1. General public services	1,492,230,462	1,456,211,268	1,821,186,354
2. Public order and safety	33,868,921	35,728,596	39,325,099
3. Education affairs and pre-schoolers education	754,004,810	821,139,287	985,721,917
4. Health affairs and services	63,700,677	72,973,243	90,997,510
5. Social security and welfare	235,170,625	262,871,191	343,352,234
6. Housing and community affairs and services	1,750,033,671	2,271,676,379	2,688,513,950
7. Recreational, cultural and religious affairs	622,669,919	981,410,967	1,136,428,570
8. Agriculture, forestry, hunting fishing affairs	43,435,476	62,761,195	71,226,824
9. Mining, manufacturing, construction affairs	269,064,067	247,951,970	342,809,179
10. Transport and communication affairs	859,599,608	811,815,646	1,044,602,171
11. Other economic affairs and services	267,700,695	317,539,978	439,736,721
12. Expenditure not classified by major groups	98,157,210	72,683,340	123,338,066

V. CONSOLIDATED GENERAL
GOVERNMENT IN THE
PERIOD 1995-1997

The consolidated general government includes a consolidated presentation of the central government budget, extra-budgetary fund financial plans and local self-government and administration unit budgets. The consolidation procedure, or a cancellation of mutual transactions between the aforementioned levels of state authority, has been conducted in accordance with an international comparative methodology, the Government Fiscal Statistics, defined by the International Monetary Fund (IMF). Data on trends in general government consolidated revenues and expenditures are true measure of the size of the public sector because they encompass all levels of state authority.

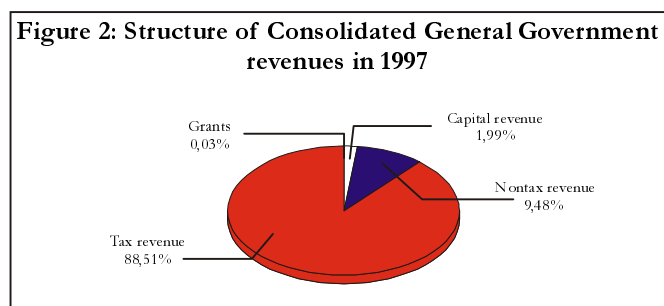
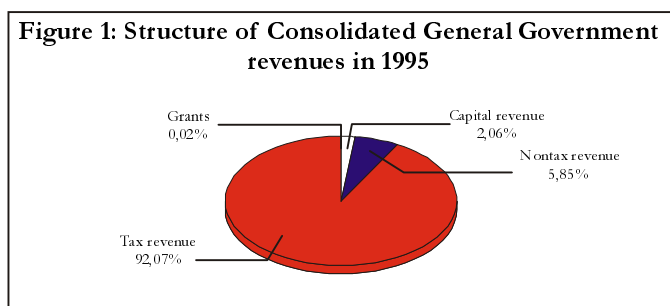
Table 1: Consolidated general government revenues and expenditures in the period 1995-1997

(in 000 HRK)	% of GDP		
	1995	1996	1997
TOTAL REVENUES AND SUBSIDIES	48.22	50.71	48.96
I. Total revenues	48.21	50.69	48.96
1. Current revenues	47.22	49.21	46.96
Tax revenues	44.40	44.72	42.34
Non-tax revenues	2.82	4.49	4.64
2. Capital revenues	1.00	1.48	0.97
II. Subsidies	0.01	0.01	0.02
TOTAL EXPENDITURES AND NET BORROWING	48.93	51.08	50.18
III. Total expenditures	48.67	50.62	49.66
1. Current expenditures	44.12	43.77	43.60
2. Capital expenditures	4.55	6.86	6.26
3. Borrowing reduced by repayments	0.26	0.45	0.52

Source: Ministry of Finance and the State Bureau of Statistics for GDP data

Table 1 shows the basic balance aggregates of the consolidated general government classified according to their economic purpose. The presented data show that a trend of sharp growth of overall public spending, measured by the total consolidated revenues and total consolidated expenditures, was partially halted in 1997. However, the preliminary data for 1998, based on trends in the consolidated central government balance sheet (central budget and extra-budgetary funds), show that it brought along a further increase in the public sector. A detailed presentation of the consolidated balance with the respective unconsolidated balances of the central budget, extra-budgetary funds and local self-government and administration is enclosed in the appendix.

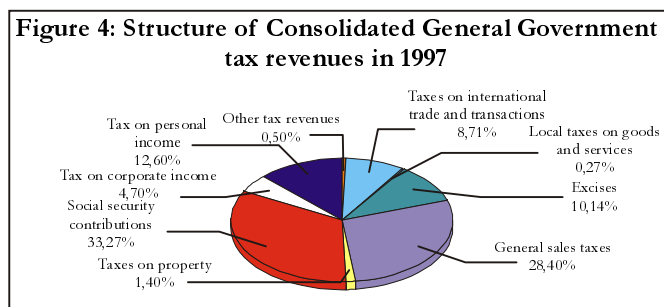
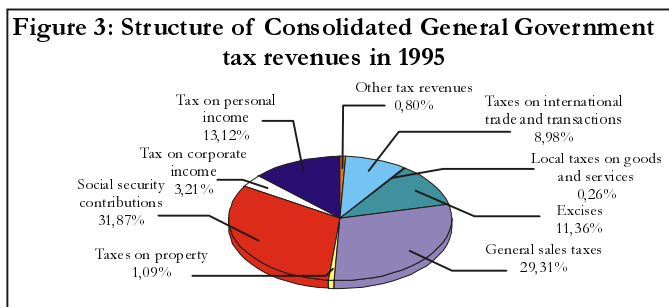
In the period under observation from 1995 to 1997, consolidated general government total revenues increased by 26.9 percent, which is the result of increases in both tax and non-tax revenues. Although non-tax revenues increased faster than the tax revenues in the observed three-year period, this did not have a more significant influence on the importance of tax revenues as the basic source of state revenues. As shown in Figures 1 and 2, the share of tax revenues in total revenues declined from 92.1 percent in 1995 to 88.6 percent in 1997.



Changes in the internal structure of tax revenues can be noted by comparing the diagrams in Figures 3 and 4. It can be seen that social security contributions and indirect taxes are the most important individual source of

tax revenues. However, in contrast to indirect taxes, the share of which has been declining in total tax revenues, the share of social security contributions has been increasing.

The overall tax burden, measured by the share of general government consolidated tax revenues in GDP, accounted for 43.4 percent of GDP in 1997, which is 1.4 percent less than in 1996. A decrease in the tax burden in 1997 was primarily the result of income tax decreases of 25 to 20 percent and a corresponding increase in the share of non-taxable income, which entered into force at the beginning of 1997. However, as already pointed out, the available but incomplete data for 1998 show that the trend of declining tax burdens did not continue in 1998. The increase of fiscal discipline, achieved by the introduction of the value-added tax, was reflected in the faster growth of tax revenues than nominal GDP in the consolidated central government balance sheets. That is why an increase of general government tax revenues can be expected in 1998 by approximately 3 percent of GDP.



Total consolidated general government expenditures show both nominal and real growth in the period under observation. During the overall period, consolidated general government expenditures grew faster than total revenues, which caused an overall deficit, although the size of the deficit was not disturbing. The consolidated general government deficit was between 0.37 percent of GDP in 1996 and 1.22 percent of GDP in 1997.

Changes in the total expenditure structure are shown in Figures 5 and 6. A tendency of increasing capital expenditures and decreasing current expenditures can be observed in the total expenditure structure. At the same time, an overall decline in current expenditure share is the result of a decline in the share of expenditures for goods and services and an increase of the share of transfers in the total expenditures. Such trends are expected and a logical consequence of the decrease in expenditures related to military purposes and an increase in expenditures related to reconstruction works (capital expenditures) as well as rising standards of living for the most socially endangered categories of the population (transfers).

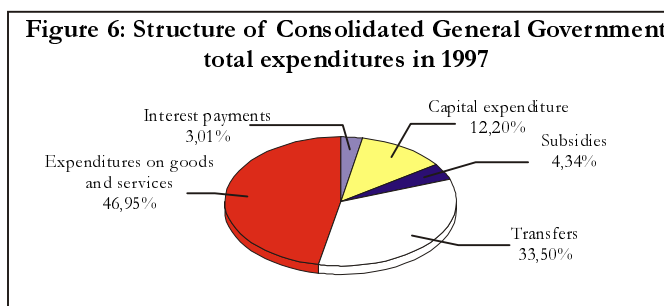
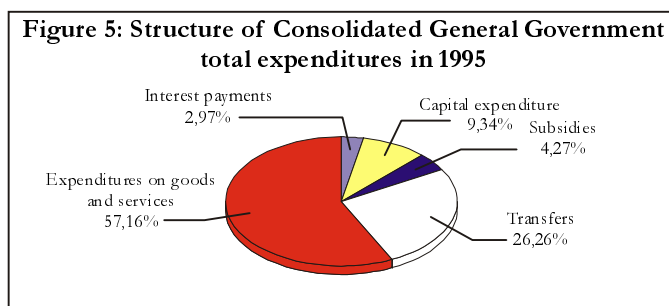


Table 2 shows the trend in the most important components of current expenditures and plainly indicates various trends in particular current expenditure categories. In the observed period, a decreasing trend in the size of expenditures for goods and services can be noticed. They were reduced from 27.82 percent of GDP in 1995 to 23.32 percent of GDP in 1997. A decreasing trend can be recorded in expenditures for salaries and wages of public sector employees in the observed three-year period as well, which were decreased from 11.83 percent of GDP in 1995 to 11.04 percent of GDP in 1997.

Table 2: Trends in consolidated general government current expenditures

	Share in GDP		
	1995	1996	1997
Expenditures on goods and services	27.82	25.32	23.32
- Wages and salaries	11.93	11.24	11.04
- Other purchases of goods and services	15.89	14.09	12.27
Interest payments	1.45	1.16	1.50
Subsidies and other current transfers	14.86	17.28	18.79

Source: Ministry of Finance and the State Bureau of Statistics for GDP data

However, expenditures for subsidies and current transfers recorded accelerated growth and increased their share in general government total expenditures from 33.67 percent in 1995 to 43.1 percent of total expenditures in 1997. In other words, the size of this type of expenditure has increased from 14.9 percent of GDP in 1995 to 18.8 percent of GDP in 1997. In the period from 1994 to 1997, current transfers and subsidies increased at an average annual rate of 24.8 percent. This growth was almost completely generated by an increase of transfers to the population, which recorded an average annual growth rate of 28 percent in the same period.

It can thus be noted that the strong growth of current transfers without a significant decrease in other general government expenditure items is a basic determinant of the accelerated growth of the state sector. Maintaining such trends in transfer movements may become a primary source of fiscal unbalance and jeopardise macroeconomic stability. Pension system as well as health insurance system reforms are the only way in which the objective of decreasing total public expenditures can be effectively ensured.

1. CONSOLIDATED GENERAL GOVERNMENT ACCORDING TO LEVELS OF FISCAL AUTHORITY

Table 3 illustrates the trends in the general government consolidated balance presented according to levels of fiscal authority. The data provided in Table 3 clearly show that the high growth of public spending by consolidated general government is a result of accelerated growth of extra-budgetary fund expenditures to the largest extent, and of an increase in local self-government and administration expenditures to a smaller extent.

Table 3: Consolidated general government according to levels of fiscal authority

(000 HRK)	Share in GDP		
	1995	1996	1997
Total revenue and grants	48.22	50.71	48.96
Budgetary central Government	28.34	29.25	27.53
Extrabudgetary Funds	15.44	15.75	15.73
1. Pension fund	8.79	8.86	8.89
2. Health fund	4.59	4.80	4.69
3. Employment fund	0.70	0.63	0.51
4. Child Benefit fund	0.79	0.82	0.79
5. Croatian Water Management fund	0.56	0.64	0.84
Local Government	4.44	5.71	5.70
Total expenditure and net lending	48.93	51.08	50.18
Budgetary central Government	26.46	25.52	23.69
Extrabudgetary Funds	18.27	19.84	20.76
1. Pension fund	9.01	9.75	11.22
2. Health fund	7.20	7.79	7.11
3. Employment fund	0.45	0.63	0.58
4. Child Benefit fund	0.83	0.80	0.82
5. Croatian Water Management fund	0.78	0.87	1.03
Local Government	4.20	5.71	5.73
Total deficit/ surplus	-0.71	-0.37	-1.22

Source: Ministry of Finance and the State Bureau of Statistics for GDP data

During the three-year period between 1995 and 1997, the central budget decreased its share in revenues from 58.77 percent in 1995 to 56.22 percent in 1997 in the structure of consolidated general government total revenues. At the same time, the constant growth of the revenue share of extra-budgetary funds in total

revenues was achieved (from 32.02 percent in 1995 to 32.13 percent in 1997), as well as growth in the share of local self-government and administration (from 9.21 percent in 1995 to 11.64 percent in 1997). The central budget share has been decreasing continually in the total expenditures of the consolidated general government (from 54.08 percent in 1995 to 47.2 percent in 1997), with the constant high growth in the share of local government expenditures (from 8.58 percent in 1995 to 11.43 percent in 1997) and extra-budgetary funds (from 37.34 percent in 1995 to 41.37 percent in 1997).

An analysis of the expenditure side of the general government consolidated balance shows that the central budget is experiencing a continuous consolidated surplus, and that the consolidated expenditures of the central budget started to decline as of 1996. The further decline of consolidated central budget expenditures continued in 1997.

However, expenditure trends in extra-budgetary funds and local self-government and administration show unequivocally that the focus of fiscal problems and public spending increases can be found in this sphere. An additional widening of the gap between consolidated extra-budgetary fund revenues and expenditures, along with the existing deficit financing methods, shows that it is extra-budgetary funds (primarily the Pension and Disability Insurance Fund and the Croatian Health Insurance Fund) which are the basic generators of the growth trend in public expenditures and consolidated deficits, which was maintained at a low level during the overall period only because of a high consolidated central budget surplus.

Therefore, the strategic aim is to halt further growth in the public sector and to embark upon a process of reducing it in the subsequent period, in accordance with the achieved level of economic development in Croatia.

Table 4 clearly shows that Croatia has a large public sector (measured by share of general government in GDP) in comparison to EU countries and transition countries. The data provided in Table 4 indicates a continuous growth trend in the size of the public sector, and this stands in complete contrast to the declining trends noticeable during the past years in developed countries and advanced transition countries.

Table 4: Total consolidated general government expenditures (% of the GDP)

	1995	1996	1997
EUROPEAN UNION			
Ireland	38.0	37.4	36.1
Great Britain	43.0	41.9	39.7
Greece	47.4	44.7	41.8
Spain	44.8	43.7	42.2
Portugal	49.7	48.4	46.9
Germany	49.5	48.9	47.7
Netherlands	51.4	49.6	49.1
Italy	52.7	52.7	50.6
Austria	52.5	51.8	50.7
Belgium	53.8	53.0	52.2
France	54.3	54.8	54.1
Finland	57.9	57.3	54.2
Denmark	56.3	55.9	54.4
Sweden	65.6	64.2	62.3
Average EU	51.2	50.3	48.7
Countries in transition			
Czech Republic ¹⁾	45.8	45.3	44.1
Poland	49.7	48.4	46.9
Hungary	49.3	43.8	42.5
Slovenia ²⁾	45.7	44.9	46.2
Croatia ³⁾	48.9	51.1	50.2
Average excl. Croatia	47.9	46.4	45.5
Average incl. Croatia	47.7	47.0	46.3

Source: OECD Economic Outlook, August 1998

¹⁾ Source: Ministry of Finance of the Czech Republic and OECD Economic Outlook, August 1998

²⁾ Source: Ministry of Finance Republic of Slovenia

³⁾ Source: Ministry of Finance and the State Bureau of Statistics for GDP data

2. TRENDS IN CONSOLIDATED GENERAL GOVERNMENT SURPLUS/DEFICITS

A decrease in current expenditures in the total expenditure structure, followed by an increase of the capital expenditure share in the observed period, indicates a tendency of slower growth in current expenditures than growth in current revenues at the consolidated general government level. The tendency of relative decrease in current expenditures in the total expenditure structure, followed by an increase in the current surplus (savings) of the general government consolidated budget in the period between 1995 and 1996 slowed down slightly in 1997, and the current expenditure share increased in the total expenditure structure. The current surplus trend is presented in Table 5.

Table 5: Current surplus of consolidated general government and level of capital expenditure coverage

Year	Current surplus in 000 HRK	Share in GDP	Capital expenditure	Coverage degree
1994	4,227,126	4.83	2,667,224	158.48
1995	3,048,771	3.10	4,472,752	68.16
1996	5,846,352	5.45	7,356,212	79.48
1997	5,387,786	4.51	7,449,672	72.32

Source: Ministry of Finance and the State Bureau of Statistics for GDP data

In the observed period, savings, measured as the difference between current revenues and current expenditures, presented the most important source of financing for state capital expenditures. Thus 68.16 percent of capital expenditures was financed by savings in 1995, and in 1996 savings covered 79.48 percent of capital expenditures, and 72.32 percent of capital expenditures of the consolidated budget in 1997.

Table 6 presents the trend in the overall surplus/deficit of the consolidated government. In the observed period between 1995 and 1997, the achieved general government consolidated budget deficit did not exceed 1.22 percent of GDP. In 1995 a deficit in the amount of HRK 699 million was incurred, which was 0.71 percent of GDP. In 1996, a consolidated budget deficit in an amount of HRK 399 million, or 0.37 percent of GDP, was incurred, while in 1997 a deficit in an amount of HRK 1,497 million, or 1.25 percent of GDP, was incurred.

Table 6: The deficit and consolidated general government deficit financing

	Share in GDP		
	1995	1996	1997
Current deficit/surplus	3.09	5.45	4.38
Total deficit/surplus	-0.71	-0.37	-1.22
Total financing	0.71	0.37	1.22
Domestic financing	-0.06	-0.49	-1.32
External financing	0.77	0.87	2.53

Source: Ministry of Finance and the State Bureau of Statistics for GDP data

VI. ORGANISATIONAL STRUCTURE OF THE
MINISTRY OF FINANCE

The Ministry of Finance is one of the five state ministries. The status of the state ministry is attributed to the Ministry of Finance as a result of the relevance of tasks performed by the Ministry of Finance in the framework of the entire government administration, and the fact that all tasks within the scope of the Ministry of Finance are performed at the centralized level for the entire state.

The organizational scheme of the Ministry of Finance is shown in the diagram 1. The head of the Ministry of Finance is the Minister of Finance. The Minister of Finance has one Deputy. The Ministry of Finance is divided between fifteen organizational units, as shown in the organizational scheme for the performance of tasks within the scope of the Ministry of Finance. The organizational units within the Ministry of Finance are as follows:

- Customs Administration
- Foreign Exchange Inspectorate
- Financial Police
- Tax Administration
- Macroeconomic Analysis and Forecasts Department
- Budget Preparation and Consolidation Department
- Budget Execution Department
- Cash and Debt Management Department
- International Financial Relations Department
- Economic Affairs Department
- Banking, Foreign Exchange and Insurance Department
- Government Accounting Department
- Information Technology and Procurement Department
- Cabinet of the Minister
- Office of the Secretary of the Ministry of Finance

Custom Administration is responsible for proposing the custom policy measures, organising the activities of the custom offices, discovering and preventing the offence against customs regulations, as well as for the performance of other tasks as requested by the Minister. The head of Custom Administration is Assistant to Minister.

Tax Administration Department is responsible for organising, co-ordinating and supervising the payments of government revenues, proposing the tax policy measures, analysing and surveying the application of tax laws as well as the functioning of the tax system. It is also responsible for the performance of other tasks as requested by the Minister. The head of Tax Department is Assistant to Minister.

Foreign Exchange Inspectorate is responsible for the supervision of foreign exchange and foreign trade operations, as well as for foreign loans arrangements and the performance of tasks as requested by the Minister. The head of Foreign Exchange Inspectorate is general foreign exchange inspector who is also Assistant to Minister.

Financial Police is responsible for the supervision of payments of government revenues as well as local government and extrabudgetary funds' revenues. It is also responsible for the performance of tasks as requested by the Minister. The head of Financial Police is general financial police inspector who is also Assistant to Minister.

Macroeconomic Analysis and Forecasts Department is responsible for the performance of macroeconomic trends analysis and forecasts, analysis of fiscal policy effects on the economy and other tasks as requested by the Minister. The head of the Macroeconomic Analysis and Forecasts Department is Assistant to Minister.

Budget Preparation and Consolidation Department is responsible for the development and preparation of government budget and extrabudgetary funds budgets, for budget consolidation, development of public revenues and expenditure trends report, drafting of laws within the financing of local government and other

tasks as requested by the Minister. The head of the Budget Preparation and Consolidation Department is Assistant to Minister.

Budget Execution Department is responsible for budget execution and the performance of administrative tasks related to budget execution, development of annual budget report documentation, performance of budgetary control with respect to ensuring legal utilisation of budgetary funds and other tasks as requested by the Minister. The head of the Budget Execution Department is Assistant to Minister.

Government Accounting Department is responsible for Treasury Ledger System, determination of government accounting standards and other tasks as requested by the Minister. The head of Government Accounting Department is Assistant to Minister.

Cash and Debt Management Department is responsible for ensuring cash management, supervision of all transactions related to government debt, keeping records of the government debt, supervision and analysis of government borrowings and other tasks as requested by the Minister. The head of the Cash and Debt Management Department is Assistant to Minister.

Government Treasury System is divided between Budget Execution Department Cash and Debt Management Department and Government Accounting Department.

International Relations Department is responsible for the preparation of legal regulations, which are related to international financial relations, performance of tasks related to negotiations on foreign loans, preparation of draft decrees on the issuance of foreign loan guarantees and other tasks as requested by the Minister. The head of International Relations Department is Assistant to Minister.

Economic Department is responsible for the surveillance and analysis of public enterprises business operations, surveillance of disasters effects and war devastation, performance of tasks related to concessions and other tasks as requested by the minister. The head of Economic Department is Assistant to Minister.

Banking, Foreign Exchange and Insurance Department is responsible for the participation in developing legal regulations related to banking, foreign exchange and insurance systems, monitoring capital market operations and the performance of other tasks as requested by the Minister. The head of Banking, Foreign Exchange and Insurance Department is Assistant to Minister.

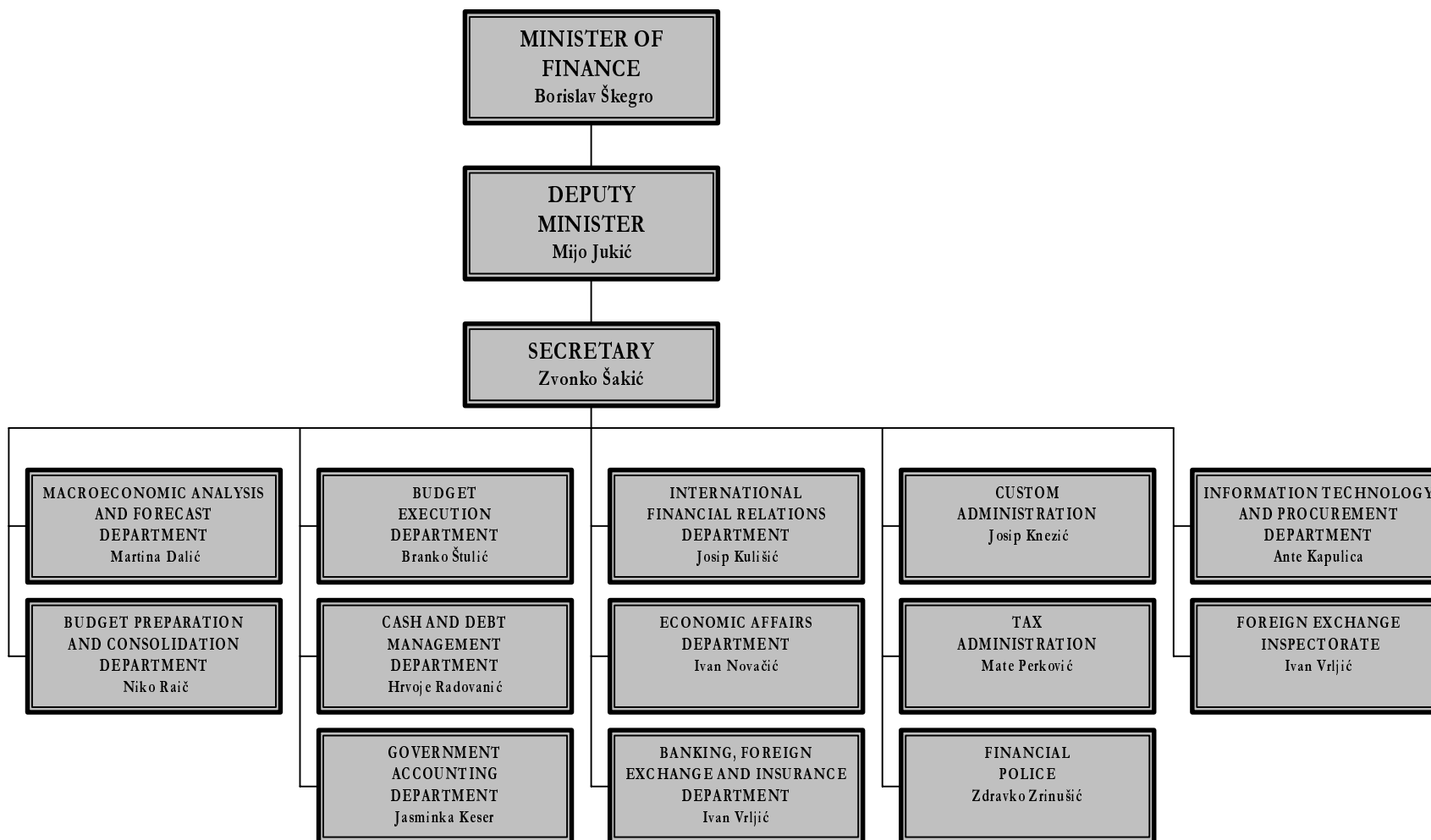
Informatization and Procurement Department is responsible for the performance of tasks related to the building and maintenance of the Ministry's computer network, public procurements, as well as for the performance of general administrative tasks and other tasks as requested by the Minister. The head of the Informatization and Procurement Department is Assistant to Minister.

The Cabinet of the Minister is responsible for the performance of protocolary tasks on behalf of the Minister and his Deputy, public relations, administrative tasks related to the communication with the Government and the Croatian Parliament and other tasks as requested by the Minister of Finance.

The Office of the Secretary of the Ministry of Finance is responsible for providing co-ordination in developing laws and other regulations within the scope of the Ministry of Finance, and for the performance of employment policy and other tasks as requested by the Minister. The head of the Office is Secretary of the Ministry.

In the end of 1998, the total number of employees in the Ministry of Finance amounted to 7,524 people employed.

THE ORGANIZATIONAL SCHEME OF THE MINISTRY OF FINANCE OF THE REPUBLIC OF CROATIA



**FORMER MINISTERS OF FINANCE
OF THE REPUBLIC OF CROATIA**

MARIJAN HANŽEKOVIĆ, Ph.d.

July 27, 1990 - August 3, 1991

JOZO MARTINOVIĆ

August 4, 1991 - August 11, 1992

ZORAN JAŠIĆ, Ph.d.

August 12, 1992 - July 6, 1994

BOŽO PRKA

July 7, 1994 - September 11, 1997

APPENDICES

Appendix 1: Basic Macroeconomic Indicators of Croatian Economy

	1994	1995	1996	1997	1998
GDP, current prices (mil. HRK)*	87,441.2	98,382.0	107,980.6	122,904.5	135,645.2
GDP growth rate, in %	5.9	6.8	6.0	6.5	2.7
GDP, current prices (mil. HRK) ⁺	14,234.1	131,371.0	143,220.0	158,974.0	179,600.0
GDP, current prices (mil. USD)	14,591.5	18,811.1	19,871.7	19,946.5	21,320.2
Retail prices, period average, %	97.6	2.0	3.5	3.6	5.7
Producer's prices, period average, %	77.6	0.7	1.4	2.3	-1.2
Cost of living, period average, %	107.2	4.0	4.3	4.1	6.4
Exchange rate HRK/USD, period average	5.99	5.23	5.43	6.16	6.36
Trade Balance (mil. USD)	-1,322.5	-3,237.5	-3,651.2	-5,224.4	-4,168.9
Current Account Balance (mil. USD)**	785.7	-1,283.8	-857.8	-2,434.0	-1,553.8
International reserves of CNB, end of period (mil. USD)	1,405.0	1,895.2	2,314.0	2,539.0	2,815.6
CNB discount rate, in %, on yearly basis	8.5	8.5	6.5	5.9	5.9
Total outstanding external debt, mil. USD ¹	3,698.5	4,213.9	4,808.4	6,661.6	8,488.7
Internal public debt, mill. HRK	...	16,405.4	16,533.7	14,608.7	13,697.5
Deficit/Surplus - Consolidated Central Government, mill. HRK	1,413.0	-883.0	-477.4	-1,586.7	882.1
Unemployment rate, % of labour force	14.5	14.5	16.4	17.5	18.6
Unemployment rate - ILO comparable, % ²	10.0	9.9	11.2
Average monthly net wages and salaries, growth rate as %	137.1	45.8	11.8	16.9	12.8
Average monthly gross wages and salaries, growth rate as %	...	34.0	12.3	13.1	12.6
Average monthly pension, growth rate as %	100.1	23.8	10.1	16.2	11.4
Total volume of industrial production, growth rate as %	-2.7	0.3	3.1	6.8	3.7
Nights spent by tourists, growth rate as %	54.8	-35.6	66.5	41.3	3.2
Area (square km)	56,538	56,538	56,538	56,538	56,538
Population, mid-year (mill.)	4.6	4.7	4.5	4.6	4.6

⁺ MF estimate based on VAT revenue

* revision by CBS

** results of the first stage of revision - preliminary

¹ London Club effect included in the whole period. New changes are results of adjustments with BOP

² CBS data from Labor Force Survey

Appendix 2: Budgetary Central Government Revenue and Grants

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total revenue and grants	23,142,632	27,980,779	31,367,481	33,846,123	43,808,593	49,047,850
II.	Total revenue	23,142,632	27,880,779	31,367,481	33,846,123	43,808,593	49,047,850
III.	Current revenue	22,788,882	27,287,119	30,244,343	33,384,986	42,019,401	44,642,150
IV.	Tax revenue	22,377,482	26,505,353	28,530,426	31,338,173	39,899,694	42,547,792
1.	Taxes on personal income	3,211,607	3,497,588	4,216,938	4,102,217	4,915,096	4,603,535
2.	Taxes on corporate income	591,585	1,009,073	1,271,183	1,785,259	2,461,149	2,936,380
3.	Taxes on real estate transactions	117,672	141,756	171,776	242,702	270,925	349,715
4.1.	Sales tax	13,107,159	12,802,257	13,504,368	15,133,172	1,972,045	650,000
4.2.	Value added tax	0	0	0	0	20,228,226	22,521,720
5.	Excises	1,813,581	4,960,440	5,390,785	5,404,837	5,767,981	6,479,746
	a) on oil products	670,441	2,559,021	2,691,840	2,728,346	3,169,771	3,626,685
	b) on alcohol	75,140	183,458	197,623	176,681	176,897	200,927
	c) on beer	128,983	266,031	262,080	279,086	277,889	331,097
	d) on beverage	51,208	108,498	108,737	110,255	83,182	96,701
	e) on tobacco products	880,466	1,759,266	2,039,532	1,999,988	1,983,435	2,139,242
	f) on coffee	0	67,642	68,704	74,959	76,807	85,094
	g) on imports of motor vehicles	7,343	16,524	22,269	35,522	128,806	139,851
6.	Taxes on international trade and transactions	3,486,771	3,922,481	3,942,438	4,639,995	4,127,523	4,333,565
6.1.	Custom duties	714,839	782,860	3,942,438	4,639,995	4,127,523	4,333,565
6.2.	Other imports charges	2,771,932	3,139,621	0	0	0	0
7.	Other taxes	49,107	171,758	32,938	29,991	27,943	533,281
V.	Nontax revenue	411,400	781,766	1,713,917	2,046,813	2,119,707	2,094,358
8.	Central bank profits	141,473	165,889	82,255	129,207	265,043	200,000
9.	Part of profits of public enterprises	44,765	142,812	134,866	329,842	351,134	800,000
10.	Revenue from interests	0	7,580	3,038	1,421	2,161	2,420
11.	Other property income	0	13,207	116,163	82,082	237,620	323,446
12.	Administrative fees and charges	25,575	49,501	510,489	562,611	532,697	119,238
13.	State administration bodies' revenue	19,876	55,370	304,702	286,830	115,994	190,618
14.	Roads' charges	0	106,200	130,939	347,086	271,762	60,716
15.	Fines and forfeits	110,547	187,584	228,547	281,011	308,147	391,270
16.	Other nontax revenue	69,164	53,623	202,918	26,723	35,149	6,650
VI.	Capital revenue	353,750	593,660	1,123,138	461,137	1,789,192	4,405,700
17.	Sales of public flats	28,456	54,740	166,683	159,420	155,169	135,500
18.	Sales of army's flats	0	43,210	401,931	157,940	201,448	165,000
19.	Revenue from privatization	325,294	495,710	554,524	143,777	1,432,366	4,100,000
20.	Other capital revenue					209	5,200
VII.	Grants	0	100,000	0	0	0	0

Appendix 3: Budgetary Central Government Expenditure and Net Lending by Economic Categories

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total expenditure and lending minus repayments	22,598,774	28,696,186	31,501,501	35,006,314	42,551,916	49,047,850
II.	Total expenditure	22,282,792	28,475,583	30,972,816	34,395,182	41,390,372	47,252,720
III.	Current expenditure	20,360,525	25,495,182	25,930,068	29,579,721	34,883,026	39,223,533
1.	Expenditures on goods and services	16,613,749	20,734,529	19,623,107	20,263,325	22,648,712	23,245,910
1.1.	Wages and salaries	6,517,586	8,393,597	8,365,211	9,147,512	10,851,793	12,098,183
1.2.	Employer contributions	1,367,573	1,716,123	1,966,383	1,892,364	2,178,503	2,587,444
1.3.	Other purchases of goods and services	8,728,590	10,624,809	9,291,513	9,223,449	9,618,416	8,560,283
2.	Interest payments	1,002,506	1,392,084	1,217,618	1,737,016	1,951,283	2,162,797
2.2.	Domestic payments	895,235	911,473	949,879	775,007	917,305	864,107
2.3.	Payments abroad	107,271	480,611	267,739	962,009	1,033,978	1,298,690
3.	Subsidies and other current transfers	2,744,270	3,368,569	5,089,343	7,579,380	10,283,031	13,814,826
3.1.	Subsidies	1,762,667	1,809,780	2,076,847	2,307,071	3,274,689	2,962,574
3.1.1.	To nonfinancial public enterprises	1,709,155	1,766,074	1,995,594	2,085,988	2,847,858	2,477,316
3.1.2.	To financial institutions	0	0	1,684	1,281	0	0
3.1.3.	To other enterprises	53,512	43,706	79,569	219,802	426,831	485,258
3.2.	Transfers to other levels of Government	330,215	842,135	1,933,068	4,041,503	5,733,307	8,495,774
3.3.	Transfers to nonprofit institutions	177,192	216,148	275,224	314,696	355,667	477,020
3.4.	Transfers to households	442,120	477,387	774,412	878,006	889,161	1,154,221
3.5.	Transfers abroad	32,076	23,119	29,792	38,104	30,207	725,237
IV.	Capital expenditure	1,922,267	2,980,401	5,042,748	4,815,461	6,507,346	8,029,187
4.	Acquisition of fixed capital assets	1,588,767	1,634,158	2,216,434	1,977,534	2,765,081	4,467,212
5.	Purchases of stocks	180,000	0	0	0	0	0
6.	Purchases of land and intangible assets	0	0	194,214	238,691	287,741	517,936
7.	Capital transfers	153,500	1,346,243	2,632,100	2,599,236	3,454,524	3,044,039
7.1.	To other levels of national government	140,000	0	100,000	113,000	770,983	555,937
7.2.	To nonfinancial public enterprises	0	194,674	270,000	434,713	544,089	414,100
7.3.	To financial institutions	0	0	0	0	0	5,000
7.4.	To other enterprises	0	0	1,480	3,100	20,642	145,241
7.5.	Other domestic capital transfers	13,500	1,144,169	2,245,820	2,036,583	2,103,810	1,913,761
7.6.	Capital transfers abroad	0	7,400	14,800	11,840	15,000	10,000
V.	Lending minus repayments	315,982	220,603	528,685	611,132	1,161,544	1,795,130
8.	To other levels of national government	0	1,141	0	43,587	12,709	95,883
9.	To nonfinancial public enterprises	0	40,675	0	-263,142	58,244	95,040
10.	To financial institutions	268,651	78,631	147,506	603,948	960,636	1,041,000
11.	Other domestic lending minus repayments	47,331	81,095	367,841	205,734	104,222	535,207
12.	Net lending abroad	0	19,061	13,338	21,005	25,733	28,000

Appendix 4: Budgetary Central Government Expenditure by Function

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I	Total expenditure	22,282,792	28,475,583	30,972,816	34,395,182	41,390,372	47,252,720
1.	General public services	1,674,965	1,911,166	1,911,595	2,182,768	3,382,441	3,725,223
2.	Defence affairs and services	7,650,165	9,910,927	7,760,190	6,990,659	7,373,239	6,087,207
3.	Public order and safety affairs	2,841,432	3,351,489	3,714,158	4,169,881	4,251,480	4,596,898
4.	Education affairs and services	2,864,662	3,277,776	3,599,830	4,050,800	4,668,772	5,933,940
5.	Health affairs and services	57,245	78,167	151,619	184,758	816,772	831,222
6.	Social security and welfare affairs and services	2,547,002	3,185,789	4,408,288	6,451,998	8,024,614	10,900,464
7.	Housing and community amenity affairs and services	462,741	1,343,216	2,602,722	2,069,451	2,620,402	2,720,510
8.	Recreational, cultural and religious affairs	308,960	430,115	410,711	539,479	576,615	945,961
9.	Agriculture, forestry, fishing, hunting affairs	652,968	511,479	550,976	616,317	1,103,215	1,163,263
10.	Mining, manufacturing, construction affairs	192,398	255,352	381,307	692,771	728,932	483,510
11.	Transport and communication affairs and services	1,498,506	2,232,489	3,404,954	3,433,519	4,073,080	5,503,049
12.	Other economic affairs and services	273,661	226,887	305,008	648,405	548,438	816,789
13.	Expenditures not classified by major group	1,258,087	1,760,731	1,771,458	2,364,376	3,222,372	3,544,684

Appendix 5: Financing by Type of Debt Holder

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total financing	-543,858	715,407	134,020	1,160,191	-1,256,677	0
II.	Domestic financing	-591,189	29,402	-669,912	-1,825,749	-1,247,563	-2,325,661
1.	From other general government	0	0	0	0	190,000	0
2.	From monetary authorities	-617,286	395,967	-152,745	-354,848	112,392	0
2.1.	CNB - net borrowing	-284,690	126,186	-233,834	-241,340	0	0
2.2.	Changes in deposits	-332,596	269,781	81,089	-113,508	112,392	0
3.	From deposit money banks	-63,832	1	-308,357	-1,357,298	-1,638,606	-1,951,644
4.	Other domestic financing	89,929	-366,566	-208,810	-113,603	88,651	-374,017
4.1.	From other financial institutions	0	25,000	10,000	-12,303	-6,860	-41,567
4.2.	From nonfinancial public enterprises	0	0	0	0	0	0
4.3.	From nonfinancial private sector	0	0	0	0	0	0
4.4.	Other domestic financing n.e.c.	89,929	-391,566	-218,810	-101,300	95,511	-332,450
III.	Financing abroad	47,331	686,005	803,932	2,985,940	-9,114	2,325,661
5.	From international development institutions	0	63,540	482,028	470,073	379,921	874,926
5.1.	Drawings	0	124,483	581,243	557,570	504,185	1,045,916
5.2.	Amortisation	0	-60,943	-99,215	-87,497	-124,264	-170,990
6.	From foreign governments	47,331	29,570	-364,330	-502,829	-525,161	-384,723
6.1.	Drawings	47,331	29,570	0	0	0	110,643
6.2.	Amortisation	0	0	-364,330	-502,829	-525,161	-495,366
7.	Other borrowing abroad	0	592,895	686,234	3,018,696	136,126	1,825,459
7.1.	Other borrowing abroad	0	592,895	686,234	-3,749	-11,809	366,709
7.2.	Supplier credits	0	0	0	0	0	0
7.3.	Other borrowing abroad n.e.c.	0	0	0	3,022,445	147,935	1,468,750
8.	Changes in cash, deposits and securities	0	0	0	0	0	0

Appendix 6: Financing by Type of Debt Instrument

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total financing	-543,858	715,407	134,020	1,160,191	-1,256,677	0
II.	Domestic financing	-591,189	29,402	-669,912	-1,825,749	-1,247,563	-2,325,661
1.	Long-term bonds	160,339	-303,255	-712,116	-1,572,385	-1,956,403	-2,245,950
1.1.	Issues	160,339	554,551	545,138	146,250	0	0
1.2.	Amortisation	0	-857,806	-1,257,254	-1,718,635	-1,956,403	-2,245,950
2.	Short-term bonds and bills	0	0	268,824	113,970	182,103	0
3.	Long-term loans n.e.c.	-273,719	79,376	-292,922	-240,642	-10,375	-59,711
3.1.	Drawings	0	340,465	0	0	0	0
3.2.	Amortisation	-273,719	-261,089	-292,922	-240,642	-10,375	-59,711
4.	Short-term loans n.e.c.	0	25,000	10,000	0	190,000	0
5.	Other liabilities	-63,832	0	-855	-183	234,720	-20,000
6.	Changes in cash, deposits, and securities	-413,977	228,281	57,157	-126,509	112,392	0
III.	Financing abroad	47,331	686,005	803,932	2,985,940	-9,114	2,325,661
7.	Long-term bonds	0	0	0	3,022,445	147,935	1,436,385
7.1.	Issues	0	0	0	3,022,445	447,935	1,436,385
7.2.	Amortisation	0	0	0	0	-300,000	0
8.	Short-term bonds and bills	0	0	0	0	0	0
9.	Long-term loans n.e.c.	47,331	154,885	830,811	-36,505	363,854	1,281,911
9.1.	Drawings	47,331	215,828	1,294,356	557,570	1,769,361	2,362,267
9.2.	Amortisation	0	-60,943	-463,545	-594,075	-1,405,507	-1,080,356
10.	Short-term loans n.e.c.	0	531,120	-26879	0	-520,903	-392,635
11.	Other liabilities	0	0	0	0	0	0
12.	Changes in cash, deposits and securities	0	0	0	0	0	0

Appendix 7: Consolidated Central Government

(000 HRK)	Outturn					Budget
	1994	1995	1996	1997	1998	1999
Total revenue and grants	35,764,743	43,283,059	48,396,602	53,345,263	65,110,652	72,007,379
Budgetary central government	23,142,632	27,980,779	31,367,481	33,846,123	43,808,593	48,217,355
Extrabudgetary funds	12,622,111	15,302,280	17,029,121	19,499,140	21,302,059	23,033,529
1. Pension fund	7,165,145	8,720,426	9,584,721	11,022,237	10,713,387	12,225,784
2. Health insurance fund	3,775,177	4,558,053	5,196,313	5,824,150	8,269,030	9,268,353
3. Employment fund	556,729	691,171	676,112	638,330	718,195	766,392
4. Child benefit fund	689,405	782,087	878,500	976,695	542,849	0
5. Public water-management fund	435,655	550,543	693,475	1,037,728	1,058,598	773,000
Total expenditure and lending minus repayments	34,262,316	44,166,098	48,874,039	54,931,935	64,228,568	71,300,884
Budgetary central government	20,732,367	26,189,262	27,591,903	29,409,442	34,125,447	37,329,853
Extrabudgetary funds	13,529,949	17,976,836	21,282,136	25,522,493	30,103,121	33,971,031
1. Pension fund	6,685,575	8,860,687	10,459,776	13,795,119	16,170,417	19,061,389
2. Health insurance fund	5,255,669	7,083,073	8,357,507	8,742,813	10,776,029	11,335,008
3. Employment fund	416,095	445,942	676,184	714,077	571,227	972,332
4. Child benefit fund	665,178	820,581	853,165	1,003,702	1,032,129	1,260,000
5. Public water-management fund	507,432	766,553	935,504	1,266,782	1,553,319	1,342,302
Total deficit/surplus	1,502,427	-883,039	-477,437	-1,586,672	882,084	-50,000
Total financing	-1,412,961	883,039	477,437	1,586,672	-882,084	50,000
1. Financing from abroad	-12,982	755,158	931,093	3,111,719	86,825	
2. Domestic financing	-1,399,979	127,881	-453,656	-1,525,047	-968,909	

Appendix 8: Revenues and Expenditures of the Pension Fund

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total revenue and grants	8,324,988	10,524,558	12,407,222	15,299,580	16,093,289	19,113,507
II.	Total revenue	8,321,836	10,192,283	11,246,813	12,675,281	12,255,305	14,287,372
III.	Current revenue	8,321,836	10,030,464	11,105,745	12,439,164	11,823,285	14,287,372
IV.	Tax revenue	8,040,501	9,807,001	10,951,042	12,243,659	11,758,242	14,215,872
1.	Social security contributions	8,040,501	9,807,001	10,951,042	12,243,659	11,758,242	14,215,872
1.1.	From employees	3,799,376	4,710,925	5,266,590	5,918,109	5,710,610	6,716,740
1.2.	From employers	3,799,376	4,710,925	5,266,590	5,918,109	5,710,610	6,716,740
1.3.	From self-employed or unemployed	180,409	236,817	293,213	343,041	327,209	523,400
1.4.	Unallocated social security contributions	261,340	148,334	124,649	64,400	9,813	258,992
V.	Nontax revenue	281,335	223,463	154,703	195,505	65,043	71,500
2.	Income from dividends and interests	281,335	223,463	154,703	195,505	65,043	1,500
3.	Other nontax revenue	0	0	0	0	75,283	70,000
VI.	Capital revenue	0	161,819	141,068	236,117	432,020	0
4.	Sales of shares and public flats	0	161,819	141,068	236,117	432,020	0
VII.	Grants	3,152	332,275	1,160,409	2,624,299	3,837,984	4,826,135
5.1.	Current grants	3,152	332,275	1,160,409	2,624,299	3,837,984	4,826,135
5.1.1.	From other levels of national government	3,152	332,275	1,160,409	2,624,299	3,837,984	4,826,135
5.2.	Capital grants	0	0	0	0	0	0
I.	Total expenditure and net lending	8,001,740	10,667,302	12,411,104	15,547,850	16,556,374	19,113,507
II.	Total expenditure	8,001,740	10,667,302	12,411,104	15,547,850	16,556,374	19,113,507
III.	Current expenditure	8,001,740	10,651,243	12,393,518	15,532,570	16,522,293	18,976,446
1.	Expenditures on goods and services	379,199	477,785	427,870	534,291	594,560	722,795
1.1.	Wages and salaries	99,365	132,769	142,824	163,699	221,918	253,000
1.2.	Employer contributions	21,580	24,129	26,626	30,742	41,504	52,118
1.3.	Other purchases of goods and services	258,254	320,887	258,420	339,850	331,138	417,677
2.	Interest payments	4,020	2,270	884	13,736	27,513	22,516
2.1.	Domestic payments	4,020	2,270	884	13,736	27,513	22,516
2.2.	Payments abroad	0	0	0	0	0	0
3.	Subsidies and other current transfers	7,618,521	10,171,188	11,964,764	14,984,543	15,900,220	18,231,135
3.1.	Subsidies	0	0	0	0	0	0
3.2.	Transfers to other levels of Government	0	0	0	0	0	0
3.3.	Transfers to nonprofit institutions	1,294,585	1,782,486	1,924,702	1,721,990	344,453	0
3.4.	Transfers to households	6,304,740	8,355,121	10,002,364	13,217,390	15,500,238	18,172,135
3.5.	Transfers abroad	19,196	33,581	37,698	45,163	55,529	59,000
IV.	Capital expenditure	0	16,059	17,586	15,280	34,081	137,061
4.	Acquisition of fixed capital assets	0	16,059	17,586	15,280	34,081	137,061
V.	Lending minus repayments	0	0	0	0	0	0
	Current surplus with grants	323,248	-288,504	-127,364	-469,107	-861,024	137,061
	Total deficit/surplus	323,248	-142,744	-3,882	-248,270	-463,085	0
VI.	Total financing	-323,248	142,744	3,882	248,270	387,802	0
1.	Financing from abroad	0	0	0	0	0	0
2.	Domestic financing	-323,248	142,744	3,882	248,270	387,802	0
2.1.	From deposit money banks	0	142,744	3,882	248,270	387,802	0
2.2.	Other domestic financing	-323,248	0	0	0	0	0

Appendix 9: Revenues and Expenditures of the Health Insurance Fund

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total revenue and grants	5,941,720	7,601,890	8,750,894	9,342,902	11,552,049	12,643,308
II.	Total revenue	5,819,357	7,252,905	8,134,192	8,560,479	9,991,014	10,778,337
III.	Current revenue	5,819,357	7,252,905	8,134,192	8,535,594	9,914,912	10,777,887
IV.	Tax revenue	5,553,362	6,959,719	7,778,910	8,417,942	9,782,595	10,505,422
1.	Social security contributions	5,553,362	6,959,719	7,778,910	8,417,942	9,782,595	10,505,422
1.1.	From employees	1,982,132	2,396,100	2,712,698	3,082,123	4,412,245	5,026,111
1.2.	From employers	1,982,132	2,396,100	2,712,698	3,082,123	4,412,245	5,026,111
1.3.	From self-employed or unemployed	182,818	271,173	308,199	325,535	376,625	385,800
1.4.	Unallocated social security contributions	1,406,280	1,896,346	2,045,315	1,928,161	581,480	67,400
V.	Nontax revenue	265,995	293,186	355,282	117,652	132,317	272,465
2.	Income from dividends and interests	0	0	0	0	2,882	3,000
3.	Other nontax revenue	265,995	293,186	355,282	117,652	129,435	269,465
VI.	Capital revenue	0	0	0	24,885	76,102	450
4.	Sales of shares	0	0	0	24,885	76,102	450
VII.	Grants	122,363	348,985	616,702	782,423	1,561,035	1,864,971
4.1.	Current grants	122,363	348,985	616,702	782,423	1,561,035	1,576,803
4.1.1.	From other levels of national government	122,363	348,985	616,702	782,423	1,561,035	1,576,803
4.2.	Capital grants	0	0	0	0	0	288,168
I.	Total expenditure and net lending	5,635,856	7,592,694	8,924,017	9,433,605	11,570,688	12,643,308
II.	Total expenditure	5,635,856	7,592,694	8,924,017	9,433,605	11,570,688	12,643,308
III.	Current expenditure	5,635,856	7,528,432	8,736,628	9,176,087	11,401,107	12,513,108
1.	Expenditures on goods and services	4,980,512	6,398,022	7,102,801	7,211,883	9,323,307	10,252,976
1.1.	Wages and salaries	1,810,416	2,580,362	2,806,889	3,353,355	3,857,567	4,221,390
1.2.	Employer contributions	380,187	509,621	566,510	690,792	794,659	862,800
1.3.	Other purchases of goods and services	2,789,909	3,308,039	3,729,402	3,167,736	4,671,081	5,168,786
2.	Interest payments	0	0	0	15,163	12,318	19,000
2.1.	Domestic payments	0	0	0	15,163	12,318	19,000
2.2.	Payments abroad	0	0	0	0	0	0
3.	Subsidies and other current transfers	655,344	1,130,410	1,633,827	1,949,041	2,065,482	2,241,132
3.1.	Subsidies	0	0	0	0	0	0
3.2.	Transfers to other levels of Government	0	0	0	0	0	0
3.3.	Transfers to nonprofit institutions	0	0	0	0	0	245,500
3.4.	Transfers to households	655,344	1,130,410	1,633,827	1,949,041	2,065,482	1,995,632
IV.	Capital expenditure	0	64,262	187,389	257,518	169,581	130,200
4.	Acquisition of fixed capital assets	0	64,262	187,389	257,518	169,581	130,200
V.	Lending minus repayments	0	0	0	0	0	0
	Current surplus with grants	305,864	73,458	14,266	141,930	74,840	-158,418
	Total deficit/surplus	305,864	9,196	-173,123	-90,703	-18,639	0
VI.	Total financing	-305,864	-9,196	173,123	90,703	18,639	0
1.	Financing from abroad	0	1,653	84,073	70,903	37,332	0
2.	Domestic financing	-305,864	-10,849	89,050	19,800	-18,693	0
2.1.	From deposit money banks	0	0	89,050	19,800	-18,693	0
2.2.	Other domestic financing	-305,864	-10,849	0	0	0	0

Appendix 10: Revenues and Expenditures of the Employment Fund

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total revenue and grants	645,729	747,171	722,042	874,645	886,375	999,000
II.	Total revenue	556,729	691,171	722,042	746,867	843,343	909,000
III.	Current revenue	556,729	691,171	722,042	746,867	843,343	909,000
IV.	Tax revenue	542,694	657,284	699,785	740,466	831,446	899,500
1.	Social security contributions	542,694	657,284	699,785	740,466	831,446	899,500
1.1.	From employees	542,694	657,284	699,785	370,233	415,723	449,750
1.2.	From employers	0	0	0	370,233	415,723	449,750
V.	Nontax revenue	14,035	33,887	22,257	6,401	11,897	9,500
2.	Other nontax revenue	14,035	33,887	22,257	6,401	11,897	9,500
VI.	Capital revenue	0	0	0	0	0	0
VII.	Grants	89,000	56,000	0	127,778	43,032	90,000
3.1.	Current grants	89,000	56,000	0	127,778	43,032	90,000
3.1.1.	From other levels of national government	89,000	56,000	0	127,778	43,032	90,000
3.2.	Capital grants	0	0	0	0	0	0
I.	Total expenditure and net lending	535,626	582,591	832,968	883,743	673,458	999,000
II.	Total expenditure	535,626	582,591	832,968	883,743	673,458	999,000
III.	Current expenditure	535,626	582,591	803,181	868,319	651,898	971,104
1.	Expenditures on goods and services	275,228	195,032	219,414	175,002	113,509	624,745
1.1.	Wages and salaries	0	0	0	34,838	47,228	68,800
1.2.	Employer contributions	0	0	0	7,111	9,635	14,175
1.3.	Other purchases of goods and services	275,228	195,032	219,414	133,053	56,646	541,770
2.	Interest payments	0	0	0	0	0	0
2.1.	Domestic payments	0	0	0	0	0	0
2.2.	Payments abroad	0	0	0	0	0	0
3.	Subsidies and other current transfers	260,398	387,559	583,767	693,317	538,389	346,359
3.1.	Subsidies	0	0	0	0	0	0
3.2.	Transfers to other levels of Government	0	0	0	0	0	0
3.3.	Transfers to nonprofit institutions	119,531	136,649	156,784	162,555	92,596	12,493
3.4.	Transfers to households	140,867	250,910	426,983	530,762	445,793	333,866
3.5.	Transfers abroad	0	0	0	0	0	0
IV.	Capital expenditure	0	0	29,787	15,424	21,560	27,896
V.	Lending minus repayments	0	0	0	0	0	0
	Current surplus with grants	110,103	164,580	-81,139	6,326	234,477	27,896
	Total deficit/surplus	110,103	164,580	-110,926	-9,098	212,917	0
VI.	Total financing	-110,103	-164,580	110,926	9,098	-212,917	0
1.	Financing from abroad	0	0	0	0	0	0
2.	Domestic financing	-110,103	-164,580	110,926	9,098	-212,917	0
2.1.	From other general government	0	0	0	0	-190,000	
2.2.	From monetary authorities	0	0	0	0	0	
2.3.	From deposit money banks	0	0	110,926	9,098	-22,917	
2.4.	Other domestic financing	-110,103	-164,580	0	0	0	

Appendix 11: Revenues and Expenditures of the Child Benefit Fund

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total revenue and grants	689,405	782,087	878,500	1,013,473	1,027,055	1,260,000
II.	Total revenue	689,405	782,087	878,500	993,473	551,855	0
III.	Current revenue	689,405	782,087	878,500	993,473	551,855	0
IV.	Tax revenue	669,285	773,444	877,429	992,289	550,640	0
1.	Social security contributions	669,285	773,444	877,429	992,289	550,640	0
1.1.	From employees	669,285	773,444	877,429	975,511	551,634	0
1.4.	Unallocated social security contributions	0	0	0	16,778	9,006	0
V.	Nontax revenue	20,120	8,643	1,071	1,184	1,215	0
3.	Other nontax revenue	20,120	8,643	1,071	1,184	1,215	0
VI.	Capital revenue	0	0	0	0	0	0
VII.	Grants	0	0	0	20,000	475,200	1,260,000
4.1.	Current grants	0	0	0	20,000	475,200	1,260,000
4.1.1.	From other levels of national government	0	0	0	20,000	475,200	1,260,000
4.2.	Capital grants	0	0	0	0	0	0
I.	Total expenditure and net lending	665,178	820,581	853,165	1,003,702	551,855	1,260,000
II.	Total expenditure	665,178	820,581	853,165	1,003,702	1,032,129	1,260,000
III.	Current expenditure	665,178	820,581	853,165	1,003,702	1,032,129	1,260,000
1.	Expenditures on goods and services	26,854	19,041	27,916	24,432	34,078	46,500
1.1.	Wages and salaries	0	0	0	0	0	0
1.2.	Employer contributions	0	0	0	0	0	0
1.3.	Other purchases of goods and services	26,854	19,041	27,916	24,432	34,078	46,500
2.	Interest payments	0	0	0	0	0	0
3.	Subsidies and other current transfers	638,324	801,540	825,249	979,270	998,051	1,213,500
3.1.	Subsidies	0	0	0	0	0	0
3.2.	Transfers to other levels of Government	0	0	0	0	0	0
3.3.	Transfers to nonprofit institutions	0	0	0	0	0	0
3.4.	Transfers to households	638,324	801,540	825,249	979,270	998,051	1,213,500
IV.	Capital expenditure	0	0	0	0	0	0
V.	Lending minus repayments	0	0	0	0	-480,274	0
	Current surplus with grants	24,227	-38,494	25,335	9,771	-5,074	0
	Total deficit/surplus	24,227	-38,494	25,335	9,771	475,200	0
VI.	Total financing	-24,227	38,494	-25,335	-9,771	5,074	0
1.	Financing from abroad	0	0	0	0	0	0
2.	Domestic financing	-24,227	38,494	-25,335	-9,771	5,074	0
2.1.	From other general government	0	0	0	0	0	0
2.2.	From monetary authorities	0	0	0	0	0	0
2.3.	From deposit money banks	0	38,494	-25,335	-9,771	5,074	0
2.4.	Other domestic financing	-24,227	0	0	0	0	0

Appendix 12: Revenues and Expenditures of the Water Management Fund

(000 HRK)		Outturn					Budget
		1994	1995	1996	1997	1998	1999
I.	Total revenue and grants	440,755	608,093	797,575	1,146,762	1,376,980	1,220,069
II.	Total revenue	435,655	550,543	688,051	1,037,728	1,058,598	773,000
III.	Current revenue	435,592	550,450	687,357	1,037,205	1,058,282	772,700
IV.	Tax revenue	146,765	172,664	197,002	224,510	125,077	0
1.	Other tax revenues	146,765	172,664	197,002	224,510	125,077	0
V.	Nontax revenue	288,827	377,786	490,355	812,695	933,205	772,700
2.	Income from dividends and interests	5,422	6,928	5,073	10,718	6,448	3,000
3.	Administrative fees and charges	283,405	346,982	454,460	731,366	838,638	723,000
4.	Other nontax revenues	0	23,876	30,822	70,611	88,119	46,700
VI.	Capital revenue	63	93	694	523	316	300
5.	Sales of shares and public flats	63	93	694	523	316	300
VII.	Grants	5,100	57,550	109,524	109,034	318,382	447,069
6.	From other levels of national government	5,100	57,550	109,524	109,034	318,382	447,069
6.1.	Current grants	5,100	57,550	109,524	0	0	281,100
6.2.	Capital grants	0	0	0	109,034	318,382	165,969
I.	Total expenditure and net lending	509,914	769,404	940,400	1,275,917	1,565,308	1,365,952
II.	Total expenditure	505,295	769,404	940,400	1,275,917	1,565,308	1,365,952
III.	Current expenditure	211,156	266,123	377,775	580,213	694,534	660,000
1.	Expenditures on goods and services	209,569	260,303	361,792	555,224	659,578	625,000
1.1.	Wages and salaries	11,864	14,926	25,243	44,671	58,323	66,250
1.2.	Employer contributions	2,482	2,851	4,896	9,135	11,989	13,650
1.3.	Other purchases of goods and services	195,223	242,526	331,653	501,418	589,266	545,100
2.	Interest payments	1,587	5,820	15,983	24,989	34,956	35,000
2.1.	Domestic payments	1,587	5,820	15,983	24,989	34,956	35,000
2.2.	Payments abroad	0	0	0	0	0	0
3.	Subsidies and other current transfers	0	0	0	0	0	0
IV.	Capital expenditure	294,139	503,281	562,625	695,704	870,774	705,952
4.	Acquisition of fixed capital assets	99,310	262,353	303,788	396,559	465,314	307,952
5.	Acquisition of land and intangible assets	2,167	1,961	2,227	6,294	9,171	8,000
6.	Capital transfers to nonfinancial public enterprises	192,662	238,967	256,610	292,851	396,289	390,000
V.	Lending minus repayments	4,619	0	0	0	0	0
	Current surplus with grants	229,536	341,877	419,106	456,992	363,748	393,800
	Total deficit/surplus	-69,159	-161,311	-142,825	-129,155	-188,328	-145,883
VI.	Total financing	69,159	161,311	142,825	129,155	188,278	145,883
1.	Financing from abroad	34,205	67,500	43,088	54,876	58,607	-55,500
2.	Domestic financing	34,954	93,811	99,737	74,279	129,671	201,383
2.1.	From other general government	4,619	1,141	62,004	40,974	12,333	95,883
2.2.	From monetary authorities	0	0	0	0	0	0
2.3.	From deposit money banks	0	96,975	40,767	33,305	117,338	105,500
2.4.	Other domestic financing	30,335	-4,305	-3,034	0	0	0

Appendix 13: Outturn of Local Government Budget

(000 HRK)	Outturn				Outturn				Budget			
	1996				1997				1998			
	Municipalities	Cities	Counties	Total	Municipalities	Cities	Counties	Total	Municipalities	Cities	Counties	Total
Total revenue and grants	1,247,143	4,589,018	786,155	6,622,316	1,066,323	5,764,609	742,705	7,573,637	1,421,324	6,791,178	836,829	9,049,331
Total revenue	1,065,426	4,516,061	526,380	6,107,867	869,914	5,584,533	536,712	6,991,159	1,097,613	6,494,216	627,377	8,219,206
Current revenue	986,864	4,277,921	516,326	5,781,111	783,845	5,201,614	533,089	6,518,547	977,437	5,979,415	609,815	7,566,667
Tax revenue	498,459	2,851,749	350,984	3,701,192	351,272	3,254,176	388,904	3,994,352	401,348	3,770,435	446,036	4,617,819
Taxes and surtaxes on personal income	358,381	2,117,539	213,981	2,689,901	234,046	2,173,318	204,448	2,611,812	266,033	2,543,629	240,934	3,050,595
Taxes on corporate income	25,319	400,409	75,210	500,938	23,991	585,072	109,806	718,868	28,711	719,193	121,917	869,820
Taxes on property	93,023	265,925	20,375	379,323	78,037	410,789	16,215	505,040	86,454	406,731	27,349	520,535
Domestic taxes on goods and services	20,136	65,707	39,105	124,948	14,184	81,318	50,363	145,865	18,851	98,213	55,836	172,900
Other tax revenues	1,599	2,170	2,312	6,082	1,015	3,680	8,073	12,768	1,300	2,669	0	3,969
Nontax revenues	488,405	1,426,171	165,342	2,079,919	432,573	1,947,438	144,184	2,524,195	576,089	2,208,979	163,780	2,948,848
Capital revenues	78,562	238,140	10,054	326,756	86,069	382,919	3,623	472,611	120,176	514,802	17,561	652,539
Grants	181,717	72,957	259,774	514,448	196,409	180,077	205,993	582,479	323,711	296,962	209,453	830,125
Total expenditure and lending minus repayments	1,168,883	4,544,404	798,114	6,511,401	1,060,828	5,677,845	740,597	7,479,269	1,406,758	6,920,164	860,406	9,187,327
Total expenditure	1,159,364	4,533,696	796,576	6,489,636	1,048,236	5,649,757	716,771	7,414,763	1,387,800	6,889,399	850,040	9,127,238
Current expenditure	704,349	3,476,685	619,384	4,800,418	628,256	4,421,340	557,460	5,607,056	805,166	5,122,293	625,763	6,553,222
Wages and salaries	145,185	516,594	48,748	710,527	119,056	652,400	61,898	833,354	151,007	815,706	79,345	1,046,058
Employer contributions	25,081	95,404	7,299	127,784	21,623	122,727	10,050	154,399	27,511	152,952	12,934	193,398
Other purchases of goods and services	326,251	827,240	153,810	1,307,301	319,054	1,015,658	168,827	1,503,540	384,163	1,270,251	187,521	1,841,935
Interest payments	1,056	5,314	2,720	9,090	2,997	41,074	3,751	47,822	3,512	67,627	3,776	74,914
Subsidies and current transfers	206,777	2,032,133	406,806	2,645,716	165,526	2,589,481	312,934	3,067,940	238,974	2,815,757	342,187	3,396,918
Capital expenditure	455,015	1,057,012	177,191	1,689,218	419,980	1,228,417	159,310	1,807,707	582,633	1,767,106	224,277	2,574,017
Lending minus repayments	9,520	10,708	1,538	21,765	12,592	28,088	23,827	64,506	18,958	30,766	10,366	60,089
Current surplus without grants	282,515	801,236	-103,058	980,693	155,589	780,274	-24,371	911,492	172,270	857,122	-15,947	1,013,445
Total deficit/surplus	78,260	44,614	-11,959	110,914	5,495	86,765	2,108	94,368	14,566	-128,986	-23,576	-137,997

Appendix 14: Consolidated General Government Revenue and Grants

(000 HRK)		Outturn			
		1994	1995	1996	1997
I.	Total revenue and grants	40,194,334	47,440,127	54,385,153	60,200,150
II.	Total revenue	40,194,016	47,430,146	54,371,483	60,182,023
III.	Current revenue	39,833,410	46,451,138	52,778,745	58,986,750
IV.	Tax revenue	37,767,041	43,677,476	47,962,322	53,282,305
1.	Taxes on personal income	5,316,629	5,731,844	6,915,910	6,714,029
2.	Taxes on corporate income	886,817	1,400,964	1,772,121	2,504,127
3.	Social security contributions	11,524,971	13,919,768	15,533,703	17,725,269
4.	Taxes on property	305,635	475,848	551,049	747,742
5.	Sales tax	13,107,159	12,802,257	13,504,368	15,133,172
6.	Excises	2,689,453	4,960,440	5,390,785	5,404,837
7.	Local taxes on goods and services	347,569	114,160	115,927	145,865
8.	Taxes on international trade and transactions	3,486,771	3,922,481	3,942,438	4,639,995
9.	Other tax revenues	233,157	349,715	236,022	267,269
V.	Nontax revenues	2,066,369	2,773,661	4,816,423	5,704,445
10.	Profits of departmental enterprises	1,792	2,954	1,306	2,593
11.	Central bank's profit	141,473	165,889	82,255	129,207
12.	Part of profits of public enterprises	45,078	143,328	134,955	331,319
13.	Revenue from interests	26,338	50,987	76,909	49,274
14.	Revenue from dividends	286,757	230,391	228,718	255,808
15.	Other property income	178,342	266,657	375,135	440,970
16.	Administrative fees and charges	550,756	794,938	2,220,703	2,895,430
17.	State administration bodies' revenue	28,771	70,030	340,720	326,053
18.	Roads' charges	162,681	176,556	217,178	360,679
19.	Revenue under the special regulations	112,610	190,984	231,064	284,226
21.	Other nontax revenue	531,771	680,948	907,479	628,887
VI.	Capital revenue	360,606	979,009	1,592,738	1,195,273
22.	Sales of fixed capital assets	358,062	949,759	1,505,029	1,121,985
23.	Sales of stocks	0	0	0	0
24.	Sales of land and intangible assets	459	15,087	47,771	32,983
25.	Capital transfers from nongovernment sources	2,085	14,163	39,938	40,305
VII.	Grants	318	9,981	13,670	18,126
26.	Grants from abroad	318	9,981	13,671	18,126
26.1.	Current grants	318	6,718	8,695	9,153
26.2.	Capital grants	0	3,262	4,976	8,973
27.	From other levels of national Government	0	0	0	0
27.1.	Current grants	0	0	0	0
27.2.	Capital grants	0	0	0	0

Appendix 15: Consolidated General Government Expenditure and Net Lending

(000 HRK)		Outturn			
		1994	1995	1996	1997
I.	Total expenditure and lending minus repayments	38,597,985	48,139,844	54,784,640	61,697,267
II.	Total expenditure	38,273,826	47,881,837	54,297,299	61,057,789
III.	Current expenditure	35,606,602	43,409,085	46,941,087	53,608,116
1.	Expenditure for goods and services	22,669,186	27,369,895	27,160,325	28,666,685
1.1.	Wages and salaries	9,063,537	11,739,444	12,051,216	13,577,429
1.2.	Employer contributions	0	0		0
1.3.	Other purchases of goods and services	13,605,649	15,630,450	15,109,109	15,089,256
2.	Interest payments	1,138,202	1,423,033	1,243,318	1,838,626
2.1.	Domestic interest payments	965,577	942,422	975,566	876,332
2.2.	Interest payments abroad	172,625	480,611	267,752	962,294
3.	Subsidies and current transfers	11,799,214	14,616,157	18,537,443	23,102,805
3.1.	Subsidies	2,065,106	2,042,674	2,345,459	2,646,925
3.2.	Transfers to other levels of national Government	0	0	0	0
3.3.	Transfers to nonprofit institutions	1,410,988	1,466,871	2,399,271	2,728,045
3.4.	Transfers to households	8,271,848	11,049,809	13,722,957	17,644,373
3.5.	Transfers abroad	51,272	56,802	69,757	83,462
IV.	Capital expenditures	2,667,224	4,472,752	7,356,212	7,449,672
4.	Acquisition of fixed capital assets	2,216,119	2,502,140	3,752,841	3,814,520
5.	Purchases of stocks	180,000	135	8,076	8,795
6.	Purchases of land and intangible assets	2,167	37,728	314,622	369,303
7.	Capital transfers	268,938	1,932,749	3,280,674	3,257,054
V.	Lending minus repayments	324,159	258,007	487,341	639,478
8.	Domestic net lending	319,540	238,946	473,976	618,174
9.	Net lending abroad	4,619	19,061	13,366	21,304
	Current deficit/surplus	4,227,126	3,048,771	5,846,352	5,387,786
	Total deficit/surplus	1,596,349	-699,717	-399,487	-1,497,118

Appendix 16: Consolidated General Government Financing by Type of Debt Holder

(000 HRK)		Outturn			
		1994	1995	1996	1997
I.	Total financing	-1,596,349	699,717	399,487	1,490,109
II.	Domestic financing	-1,565,115	-56,811	-530,293	-1,619,391
1.	From other general government	0	0	0	0
2.	From monetary authorities	-617,286	395,967	-152,745	-354,848
3.	From deposit money banks	-301,679	96,484	-172,258	-1,127,563
4.	Other domestic financing	-646,150	-549,262	-205,289	-136,980
4.1.	From other financial institutions	2,515	27,515	11,985	13,154
4.2.	From nonfinancial public enterprises	0	0	3,239	5,057
4.3.	From nonfinancial private sector	-2,950	-2,950	-348	-52,707
4.4.	Other domestic financing - n.e.c.	-645,716	-573,828	-220,166	-102,485
III.	Financing abroad	-31,234	756,528	929,780	3,109,500
5.	From international development institutions	-60,313	132,693	609,189	595,852
6.	From foreign governments	47,331	29,570	-364,330	-502,829
7.	Other borrowing abroad	0	592,895	686,234	3,018,696
8.	Changes in cash, deposits and securities	-18,252	1,370	-1,313	-2,219

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