

Croatia's trade in the new age of protectionism

The significance of trade for Croatia's recent remarkable growth story

Ever since Croatia joined the EU in 2013, its trade openness index has increased for every consecutive year, apart from the pandemic year of 2020. In 2015 the index value for Croatia has surpassed that of the EU for the first time and kept rising to its current level of 124.5% versus 106% recorded for the EU-27 (Our World in Data, 2024). Trade integration has significantly propelled growth and employment over the last decade, while also allowing for the steady reduction of external debt as a percentage of GDP, which stood at 75.2% in Q3 2024 and was down from its highs of 113% in 2013 (Croatian National Bank, 2024).

The total value of goods and services exported rose by staggering \$14.57 billion, from \$34.24 in 2019 to \$48.81 in 2023.¹ While trade has not been the only factor contributing to growth, as personal consumption and fixed capital investment powered by major net transfers from the EU budget and personal remittances played an ever more prominent role, it has still acted as a powerful tailwind. Recent empirical research shows that Croatia's growth is deeply related to the dynamics of international trade and trade multiplier is generally a good predictor of the actual long-run growth rate (Srdelić and Dávila-Fernández, 2024).

All of the above mentioned factors set Croatia's growth in a league of its own versus other 26 EU member states, as measured by cumulative change in GDP growth of 19% over the period from Q4 2019 until Q3 2024 (Kral, 2024a). Strikingly, this cumulative growth was three times higher than the average growth rate for the EU-27 and is even higher than that of the USA.

¹ Author's calculation based on TradeMap data: <https://www.trademap.org/Index.aspx>.

In 2025 exports of goods are forecast to keep growing solidly, despite relatively weak demand growth in Croatia's main trading partners such as Germany, Austria and Italy. On the other hand, exports of services is expected to slow down a bit due to rising cost pressures in the travel sector. Overall, the contribution of net exports to growth in 2025 is expected to turn negative, in a context of strongly expanding domestic demand (European Commission, 2024).

The degree of Croatia's trade vulnerability to growing international protectionism

Overall, Croatia is relatively shielded from the direct effects of brewing trade wars globally as 67.77% of goods and 64.24% of exported services is destined towards the EU' Single Market, providing a significant cushion to the potential escalation of trade war in the Asia-Pacific region between the USA and China (very high likelihood), as well as in the Atlantic region between the EU and the USA (less likely, as explained in the last section).² Notwithstanding the latter scenario of a direct trade confrontation between transatlantic partners, or of EU's significant trade and geopolitical alignment with the USA against China, Croatia is only partially exposed to retaliatory US and Chinese tariffs. This can be inferred from *Table 1*, which shows the share of both imports and exports of goods and services generated by US-Croatia and China-Croatia bilateral trade in total trade over the 2019-2023 period.

² Author's calculation based on TradeMap data: <https://www.trademap.org/Index.aspx>.

Table 1 Relative importance of trade in goods and services with the USA and China

Exports of goods (share in %)	2019	2020	2021	2022	2023
USA	2.70%	3.07%	3.27%	0.23%	2.56%
China	0.71%	0.57%	0.48%	0.36%	0.34%
Import of goods (share in %)	2019	2020	2021	2022	2023
USA	0.67%	0.76%	2.02%	7.56%	2.70%
China	2.87%	4.65%	3.60%	3.28%	3.24%
Imports of services (share in %)	2019	2020	2021	2022	2023
USA	3.54%	2.75%	0.30%	5.13%	4.15%
China	0.89%	0.82%	0.61%	0.68%	0.62%
Exports of services (share in %)	2019	2020	2021	2022	2023
USA	2.88%	2.28%	3.32%	0.35%	4.56%
China	0.28%	0.17%	0.02%	0.13%	0.14%

Source: Author's calculation based on TradeMap data

In the scenario whereby US President Donald Trump slaps tariffs on the EU exports of goods due to no deal on rebalancing transatlantic trade, that would directly affect only 2.5-3% of Croatian export in goods heading to the USA. On the other hand, services are less amenable to trade restrictions, especially personal and business travel services which make up approximately two-thirds of Croatia's exported services valued at \$24 billion in 2023.³

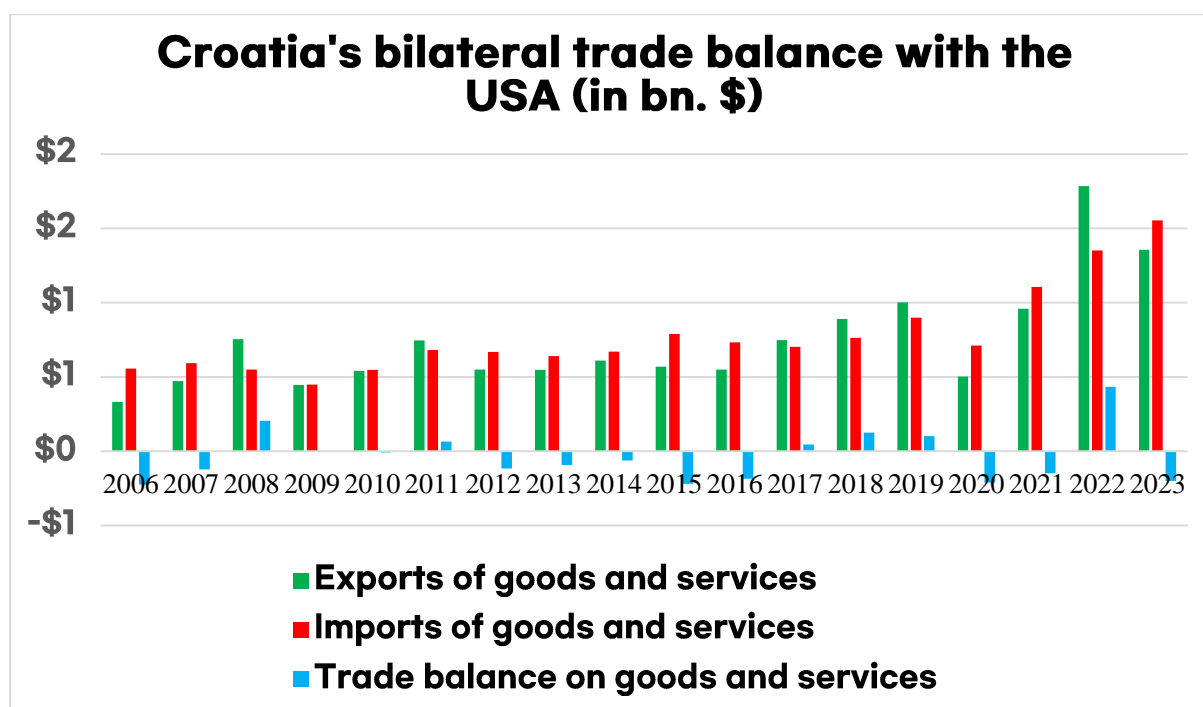
There are two sectors in the EU's export machine which solely account for roughly 40% of the EU's trade surplus in goods with the USA, totalling 1.5% of EU's GDP. The first one encompasses vehicles, boats, aircraft and trains on the one hand, while the second one covers pharmaceutical products (Kral, 2024b). Currently, most of the products listed above, which are also the ones with highest value-added share, are subject to minimal or no tariffs. For example, pharmaceutical products, machinery, and electronics have effective tariff rates of 0% (FitchRating, 2024). Under the scenario where those two sectors are most heavily affected by potential US tariffs, the most exposed Croatian products

³ Author's calculation based on TradeMap data: <https://www.trademap.org/Index.aspx>.

would be pharmaceutical products valued at \$224 million, which make up 35% of Croatian exports to the USA. Electrical machinery valued at \$104 million could also be at risk. Interestingly, Croatia's trade with the USA, as compared to trade with China has gotten bigger over time. This stands in stark contrast to the global trend according to which China supersedes the USA as the main trading partner for more than 120 states worldwide (Green, 2023).

In 2023, US-Croatia trade amounted to \$3.17 billion in comparison to China-Croatia trade of only \$1.54 billion. *Figure 1* shows the evolution of US-Croatia bilateral trade since 2006 and in most years Croatia has incurred small surpluses. The only major outlier was 2022 when the USA posted a significant surplus due to Europe's energy crunch amidst Russia-Ukraine war, which ramped up Croatia's imports of US petroleum gas and other gaseous hydrocarbons. In 2023 Croatia procured 41% of gas from the USA and the trend of rising hydrocarbons imports will continue in the coming years as Croatia is poised to position itself as an energy hub for Central Europe. This was also reiterated by Prime Minister Plenković when he was recently outlining Government's steps to bolster infrastructure expansion, including the gas connection with Slovenia, Hungary, the southern interconnection to Bosnia and Herzegovina and the direction to the west that goes from Slovenia to Austria and Bavaria. Similarly steps are made also with regard to Adriatic oil pipeline (Government of the Republic of Croatia, 2024).

Figure 1



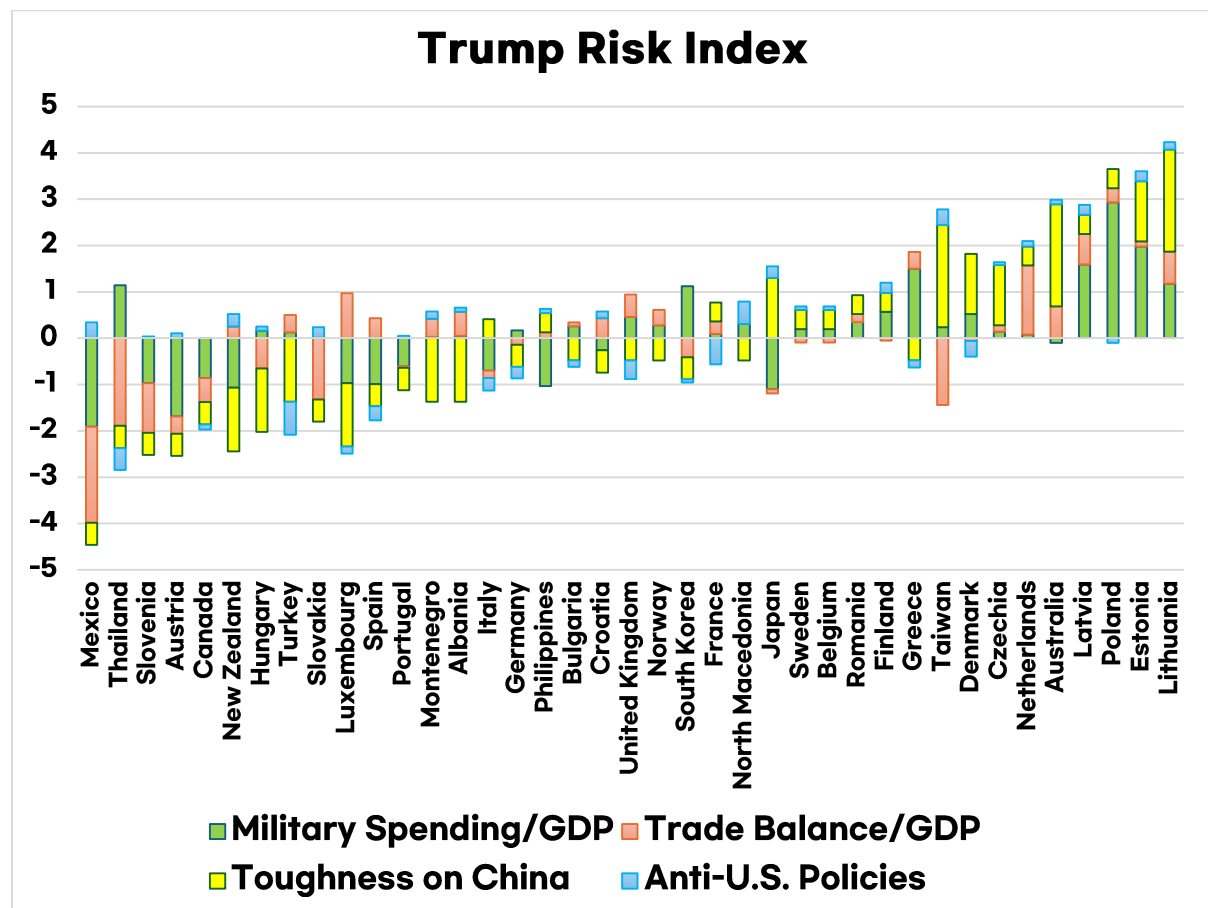
Source: Bureau of Economic Analysis

Nevertheless, even in the scenario of rocky transatlantic relations not all countries would be affected in the same way and US administration would certainly differentiate countries which it deems as the most “free-riding nations“. Information Technology and Innovation Foundation (ITIF), a Washington-based think-tank calculated Trump Risk Index (TRI) based on four indicators spanning: defense spending, trade balance, a composite of measure of anti-U.S. trade and technology policies (such as digital taxes) and the willingness to resist China’s techno-economic predation (Atkinson and Long, 2024).

On a scale from -5 to 5, where negative score represents higher risk of US tariffs, Croatia's TRI score puts it just in the middle of a 40 country sample, as shown in *Figure 2*. The negative scores are recorded for the indicators of defense spending (-0.26) and toughness on China (-0.48). In that regard Croatia has a plenty of room to alleviate US concerns by raising its defense spending towards the NATO's shared commitment of 2% of GDP and change its ambivalent stance towards the rising China's imports in the EU, which was visible in Croatia's

“abstained” vote on the European Commission's proposed tariffs on Chinese EVs. Therefore, Croatia could avoid US tariffs without much sacrifice to its bilateral trade, while being protected from China's backlash due to limited trade exposure, as shown in the next paragraph.

Figure 2



Source: Information Technology & Innovation Foundation

In second other scenario, whereby there is a growing coalescence between Washington and Brussels on the need to jointly mitigate China's industrial overcapacity flooding the global markets, Chinese retaliatory tariffs directed at Croatian exports as part of the EU's exports oriented towards China would have negligible effect on Croatia. Namely, the total value of exports of goods to China equaled paltry \$85 million in 2023, with wood and articles of wood comprising 43% of the total. China is also a trivial market for the exports of Croatian services,

totalling 0.14% of all services exported in 2023. Despite of the fact that China has shown a penchant for economic coercion measures and has beefed up its economic statecraft framework recently, if inclined to use imports as a coercion tool against Croatia, it has a limited leverage. Croatia's share of imports of goods stemming from China was 2.70% in 2023, while the share of imports of services came at paltry 0.62%.

Transatlantic alignment and China's industrial overcapacity: what is at stake for Croatia?

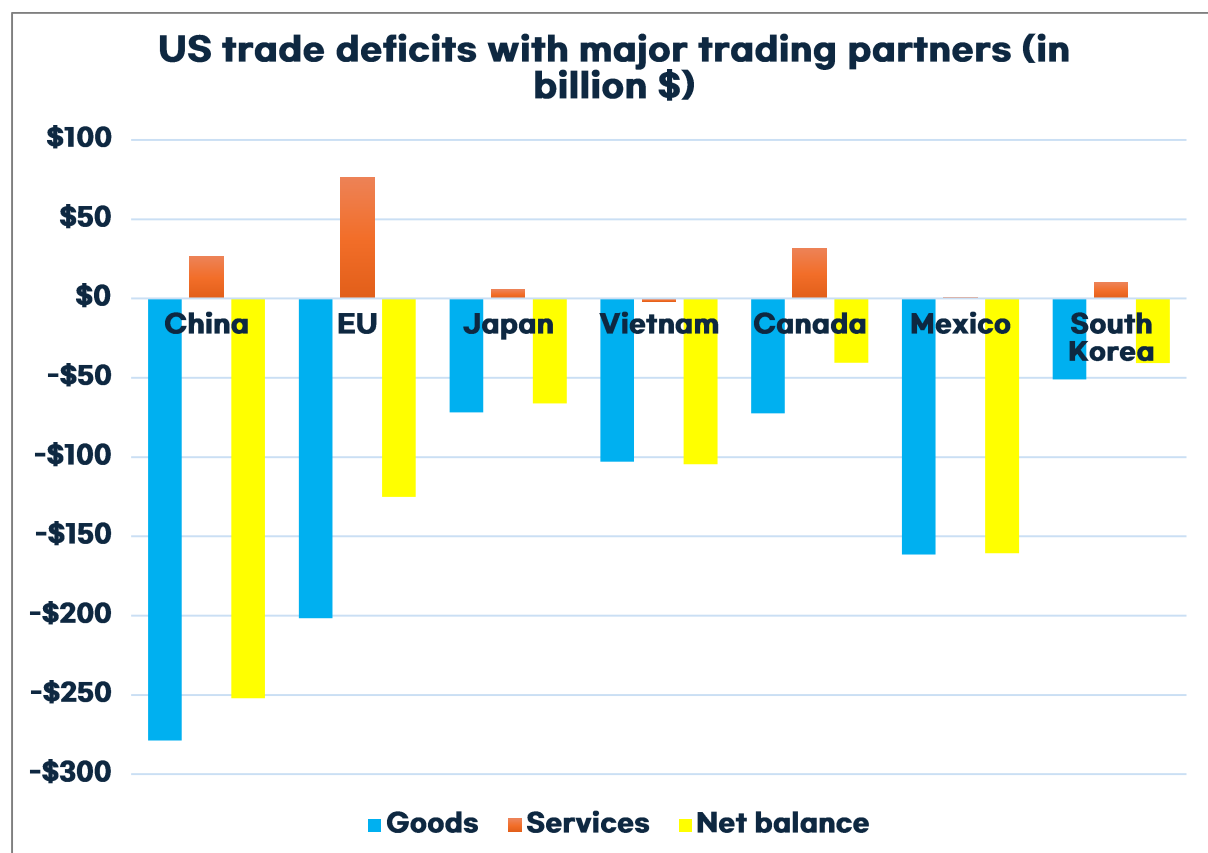
The scenario of US-EU trade alignment seems to be in the cards, despite both sides holding some grudge against each other. On the one hand Europeans are certainly jealous of US tech champions which propelled US remarkable growth while the EU missed an early opportunity to embark on the train of digital innovation. On the other hand, Americans are frustrated with the EU's systemic neglect of defense spending. However, a deal seems to be coming and Trump's tariff bluster probably acts as a negotiation tool. This was put on full display three weeks ago when President-elect Donald Trump wrote on social media: *I told the European Union that they must make up their tremendous deficit with the United States by the large scale purchase of our oil and gas. Otherwise, it is TARIFFS all the way!!!* (Oliver, 2024). Fortunately, the EU needs the US gas to wean itself off from the Russian gas, which is still at 18% of EU consumption, regardless of several rounds of Russia-targeted energy sanctions (Hockenos, 2025). Furthermore, European leaders have finally realized that they have to up the ante on NATO military spending (Peseckyte, 2024).

The final reason for optimistic perspective on US-EU relations is to be found in the fact that the EU still has a very powerful trump card up its sleeve to respond to Washington's escalation attempts. EU's dependencies are large, but strategic dependencies balance in favour of the EU. The USA relies on the EU for 32

strategically important import products, mainly in the chemical and pharmaceutical sectors, while the EU relies on only 8 US products, among which beryllium plays the most prominent role (Dewitte and Fechner, 2024).

However, the most important trump card preventing trade escalation is a destructive tit-for-tat scenario, as both sides would suffer under it. In the public discourse there is a blind spot for trade in services. While the EU is vulnerable to Trump's tariffs on goods since the EU posted \$200 billion trade surplus in 2023, the USA would be heavily exposed to the EU's trade restrictions on its \$73 billion trade in services surplus. Big US tech companies such as Meta and Alphabet would hardly reconcile themselves with diminished profits stemming from digital taxes in the lucrative EU market. In that regard, the USA has less of a leverage against the EU, as compared to its other large trade partners, as can be glimpsed from *Figure 3*.

Figure 3



Source: Bureau of Economic Analysis

Therefore, Croatia currently seems relatively isolated from the rising trend of protectionism globally, as can be visible from data presented in *Table 1*. Indeed, Croatia has a very limited trade exposure to China, while USA-Croatia trade is relatively balanced, with a perspective of further improvement due to rising imports of US gas, which would please Donald Trump's administration. Even in the case of 20% US tariffs on its exports, which could be avoidable by the virtue of increased military equipment purchases from the US arms corporations, it would still be able to navigate the storm gracefully. However, it is not isolated from the indirect and long-term consequences of the key structural change in the global economy over the last 20 years, the gigantic concentration of manufacturing in China. Hence, greater US-EU economic cooperation would enable greater market integration conducive to developing large economies of scale, which plays an indispensable role in crafting a strong and competitive position vis-à-vis China's hypercompetitive exports. Croatian producers and exporters would also profit from this broader US-EU cooperation as they would be able to significantly expand their production and act as an important hub in re-shoring and friend-shoring initiatives within fragmenting geopolitical landscape. Lower costs of production compared to more mature economies would bolster this trend.

Apart from the threat of rising asymmetric dependencies on certain categories of Chinese products such as magnesium or active pharmaceutical ingredients, which would come to the fore in the scenario of China's invasion of Taiwan, there is also a more latent and grinding threat of the EU's deindustrialization. The continued erosion of EU corporations' share of the China market, the erosion of market share in developing countries, as well as the China's industrial overcapacity coming to the EU shores, would deepen the EU's economic malaise. In this case Croatia would not be spared from hardship as its export of goods and services to key EU trading partners would seriously suffer. Therefore, finding a common and workable EU strategy to raise its

competitiveness, which also means a temporary increase of tariffs on Chinese subsidized goods, is a *condition sine qua non* of the EU's economic survival. Croatia's economic survival is inextricably linked to this pursuit.

Executive summary:

Since Croatia joined the EU in 2013 it significantly increased its trade openness, which contributed to its remarkable economic growth, especially after the COVID-19 pandemic. Two-thirds of Croatian imports and exports is destined or comes from the EU which acts as a buffer. In the context of rising global power competition and protectionism, Croatia's exports are relatively shielded as Croatia has a very limited trade dependence on China. On the other hand, its bilateral trade with the USA is on the rise and relatively balanced. There are remedies which Croatia could use to alleviate the threat of Donald Trump's administration tariffs and spare its exports to the US market. Those are increased purchases of US military equipment and energy products and the same remedies could be easily used by the EU as a whole. On the other hand, the biggest threat to Croatia's and EU's economic prosperity lies in the Chinese industrial capacity which threatens to deindustrialize the continent. The EU has to increase its competitiveness and prevent a surge in Chinese imports.

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