S&P Global Ratings

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Research Update:

Croatian City of Zagreb Affirmed At 'BBB+'; Outlook Remains Positive

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Overview

- Zagreb is posting solid budgetary performance amid robust tax revenue, which has also contributed to a strong liquidity position.
- The city is pursuing an ambitious investment agenda, and its financing plans rely on ample EU funds alongside limited recourse to debt.
- We affirmed our ‘BBB+’ long-term ratings on Zagreb.
- The outlook remains positive, reflecting our view that Zagreb's creditworthiness could strengthen further if prudent financial management practices are firmly embedded, or if financial metrics prove substantially stronger than we currently project.

Rating Action

On Sept. 19, 2025, S&P Global Ratings affirmed its 'BBB+' long-term foreign and local currency issuer credit ratings on the Croatian capital city of Zagreb. The outlook on the rating remains positive.

Outlook

The positive outlook reflects our view that Zagreb's creditworthiness could improve further if financial management practices are strengthened, or the city's debt-to-consolidated operating revenue ratio declined alongside better-than-expected budgetary performance metrics.

Downside scenario

We would revise the outlook to stable if Zagreb's fiscal profile builds up substantial imbalances, tax revenue growth falters, and budgetary performance consequently deteriorates, or the city's management fails to sustain improvements in liquidity and debt management.

Upside scenario

We could raise the ratings on Zagreb within the next 12 months if we observe the ongoing improvements in financial management practices becoming further entrenched, for example in the governance of government-related entities (GREs). Pronounced deleveraging at the city and its main GREs--possibly alongside stronger-than-expected budgetary performance--could also lead to an upgrade.

Rationale

Our positive outlook reflects the potential for further sustained improvement in Zagreb's financial management and metrics. We expect the city's debt dynamics to be shaped by the evolution of its ambitious public investment program, with borrowing mainly to co-fund projects supported by ample EU funds. If currently favorable dynamics--buoyed by tax revenue growth and external funds--weaken, the recent expansion of operating expenditure and Zagreb's limited own revenue flexibility could, however, ultimately complicate the city's budget policy.

Our ratings on Zagreb reflect the city's strong liquidity position, with substantial funds in cash and deposits well in excess of its annual debt-service requirements. These cash holdings have continuously increased over the past few years. They reflect the city's strong financial performance in recent years, but also efforts to strengthen liquidity management and reduce financial risks emanating from the city's GREs.

We also consider Zagreb's expanding economy and continued integration and convergence with the EU. We think the city's gradual alignment with EU standards over recent years has contributed, for example, to lower use of off-balance sheet debt and stronger oversight, not least given the strong push for EU-funded investments.

A robust economy and improving institutional settings support Zagreb's credit profile

Zagreb is Croatia's capital and its dominant economic center. The city contributes over one-third of Croatia's GDP, and its economic structure is more diversified than the national economy, where tourism is dominant, with Zagreb's GDP per capita well above the national average.

Resilient growth of Croatia's economy translated into robust double-digit tax revenue growth for Zagreb in the first half of 2025. We project more moderate tax revenue growth from 2026 and anticipate that the city's economy will expand in tandem with the national economy, for which we project about 3% GDP growth in 2025-2028. Robust growth in personal income tax receipts has helped mitigate surging operating expenditure, including from higher public-sector wages in Zagreb and Croatia as a whole, in turn mirroring inflation rates that exceed the eurozone average.

Despite the risk of expenditure pressures, the aggregate financial situation of Croatian municipalities, as reflected in their cash position, has been strong in recent years, owing to robust tax revenue. This is despite recent rounds of tax reform. Since January 2024, each city can determine its own personal income tax (PIT) rate within certain ranges, which were adjusted downward as of January 2025. Zagreb charges the maximum permitted tax rate. As of 2025, the central government has introduced a property tax that effectively transforms the previous holiday-homes tax. We expect this could bolster Zagreb's tax revenue and become an important policy tool for the city's housing market, a key political topic.

Frequent changes to the intergovernmental framework still hamper predictability for local governments in Croatia, despite tax reforms following a general approach of reducing labor taxation in favor of taxing property. The alignment with EU standards has, over time, strengthened the oversight of municipal finances and supported, for example, a reduction in recourse to off-balance-sheet funding operations. Coupled with a strong push for EU-funded investments and the requirements attached, this should strengthen transparency and accountability standards for local governments. These gradual improvements are reflected in our assessment of the institutional framework for Croatian municipalities, which we still view as evolving and unbalanced.

The central government has in recent years helped the city address the pandemic and the energy crisis, and is contributing to earthquake reconstruction in Zagreb. Another important source of financial support for Croatia's capital has been the EU, through the European Solidarity Fund. The city has access to favorable funding from European promotional banks to finance EU-funded projects, thus supporting its investment agenda. We also note that Zagreb and the central government are implementing several infrastructure projects in close coordination and with a substantial contribution from the state budget.

Zagreb's current administration, in office since 2021, has made significant strides to improve the city's financial management practices. For example, liquidity and liquidity management have substantially improved. Management of key municipal enterprises has been changed, with the aim of improving oversight and reducing risk. Fiscal prudence and limiting debt accumulation remains a goal, but this might be tested if tax revenue growth were to cool, given significant cost and salary increases, and substantial investment needs. We note as positive successful efforts to settle liabilities between city companies and to end past practices of funding via off-balance-sheet transactions. However, the track record is relatively short and it remains to be seen whether improvements will be sustained through political cycles. Given the dependence of Zagreb's finances on decisions made at the national level, good relations with the central government remain crucial for the city. This is especially true if party affiliations of the administration are different, as is currently the case. However, we understand there have been no major frictions recently.

Zagreb's ambitious investment agenda will shape its budget and debt trajectory, while liquidity is set to remain robust

We project that Zagreb will continue to post strong operating results over 2025-2027, with an average operating budget surplus of 12% of operating revenue. Income tax revenue growth has been particularly robust at almost 15% in the first half of the year, reflecting rising employment and salaries in the city. Although we expect strong tax revenue growth to continue in the next two-to-three years, we believe operating expenditure will also rise, due to higher costs of materials, personnel expenditure, and subsidies for items such as public transport. This should lead to a slight moderation of operating budget surpluses through 2028. At the same time, we project sizable investment spending will cause deficits after capital accounts from this year, but this will depend crucially on the pace of projects. We understand that Zagreb's investment spending is tied to EU-funded projects and corresponding financing from European promotional banks, for example a €207 million loan from the European Investment Bank (EIB).

The city will draw on its EIB loan, depending on the progress of projects, and this will be a key determinant of Zagreb's debt trajectory in the coming years. Zagreb has a sizable public investment agenda, aiming to address substantial investment needs in various areas. These comprise, for example, public buildings and road infrastructure, education, transport, stadiums and culture facilities, housing, and, politically important, wastewater treatment. In many of these investment areas, EU funds will cover a substantial part of the expenditure. Therefore, we expect the increase in the city's tax-supported debt will be contained to about 61% of operating revenue in 2027, after 53% in 2024. That said, we note the debt ratio could be lower than we currently project if investments are made more slowly than planned.

We include the debt of Zagreb’s key municipal companies, ZGH and ZET, in our calculation of the city's tax-supported debt, which includes the debt of various municipal companies and nontraditional financing like factoring. We understand the city has, for the most part, already terminated past off-budget financing practices and supports ZGH's further deleveraging.

Direct debt accounts for less than a quarter of the city's tax-supported debt, given the past use of nontraditional means like factoring and historically substantial borrowing by municipal companies. Zagreb’s direct debt consists of loans from domestic banks for investment projects and small amounts of short-term debt, but we think direct debt will increase as the city borrows from European promotional banks like the EIB to finance its investment agenda.

We regard the city's contingent liabilities as low overall, given that the debt of ZGH and ZET is already reflected in our tax-supported debt calculation. Contingent liabilities include potential further spending on earthquake-related repairs to private buildings, liabilities of other GREs apart from ZGH and ZET, and some litigation risks. By law, Zagreb needs to cover 20% of the costs of rebuilding private buildings more heavily damaged by the earthquake in 2020. The costs are hard to estimate, but effective drawings on Zagreb's finances have been well below budgeted funds so far, which we believe is likely to continue. In our view, the city might support ZGH and ZET by absorbing additional payables from the two companies or by injecting capital.

We continue to view Zagreb's budgetary flexibility as limited because large parts of the revenue structure depend on the central government's decisions. Following the income tax system reforms of 2024 and 2025, the city has set the highest rates permissible to protect its revenue, with no flexibility to adjust the rate upward. Further flexibility is therefore currently limited to certain municipal fees and taxes, which together account for less than 20% of the city's income. The introduction of property tax grants additional, albeit only limited, revenue flexibility to Zagreb. The city's spending flexibility is also constrained by the need to subsidize municipal companies ZGH and ZET, both of which supply essential public services. ZGH is responsible for gas distribution and supply, water supply and sewerage, road maintenance, waste disposal, and real estate projects. We do not think asset sales can provide substantial additional room to maneuver in the near term.

Zagreb's liquidity position has improved significantly over the past three years. Cash on hand amounted to almost €200 million on average in July 2025, comfortably covering the next 12 months' debt service and financing needs. We think cash balances could slightly fluctuate in 2025-2026, depending on the timing of loan drawings and payments for investment projects, but will likely stay at around €200 million because we understand the city aims to maintain a liquidity buffer. The city has reduced overdue payables to a negligible amount, which improves visibility with respect to its liquidity needs. We view Zagreb's access to external liquidity as satisfactory because the city has access to a pool of international banks willing to provide loans, while Croatia's eurozone accession has further improved Zagreb's capital market access.

City of Zagreb Selected Indicators

Mil. EUR	2022	2023	2024	2025bc	2026bc	2027bc
Operating revenue	1,198	1,329	1,591	1,744	1,786	1,821
Operating expenditure	1,020	1,104	1,261	1,510	1,580	1,637
Operating balance	178	225	330	234	207	185
Operating balance (% of operating revenue)	14.8	16.9	20.7	13.4	11.6	10.1

City of Zagreb Selected Indicators

Capital revenue	8	187	268	185	171	101
Capital expenditure	158	197	507	503	515	319
Balance after capital accounts	28	215	92	(84)	(137)	(33)
Balance after capital accounts (% of total revenue)	2.3	14.2	4.9	(4.3)	(7.0)	(1.7)
Debt repaid	220	170	60	95	59	49
Gross borrowings	130	83	42	164	196	82
Balance after borrowings	(62)	128	74	(15)	0	(0)
Direct debt (outstanding at year-end)	323	235	217	286	423	456
Direct debt (% of operating revenue)	27.0	17.7	13.6	16.4	23.7	25.0
Tax-supported debt (outstanding at year-end)	1,285	1,124	1,051	1,145	1,308	1,368
Tax-supported debt (% of consolidated operating revenue)	82.7	65.8	53.2	53.6	59.8	61.4
Interest (% of operating revenue)	0.5	0.4	0.3	0.5	0.5	0.5
Local GDP per capita ($)	30,610.7	36,134.9	39,629.9	43,007.4	46,345.1	50,136.8
National GDP per capita ($)	18,465.3	21,868.7	23,967.1	26,009.8	28,028.0	30,321.2

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. EUR--euro. $--U.S. dollar.

City of Zagreb Rating Component Scores

Key rating factors	Scores
Institutional framework	4
Economy	3
Financial management	4
Budgetary performance	3
Liquidity	1
Debt burden	3
Stand-alone credit profile	bbb+
Issuer credit rating	BBB+

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "**Methodology For Rating Local And Regional Governments Outside Of The U.S.**," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

- Croatia 'A-/A-2' Ratings Affirmed; Outlook Positive, Sept. 12, 2025

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Institutional Framework Assessments For Local And Regional Governments Outside Of The U.S., Sept. 10, 2025
- Sovereign Risk Indicators, July 7, 2025. Interactive version available at http://www.spratings.com/sri
- Subnational Government Outlook Mid-Year 2025: Setting Sail In A Gale, July 2, 2025
- Global Ratings List: International Public Finance Entities July 2025, July 1, 2025
- Croatian Municipalities' Transparency Benefits From Eurozone Accession, March 25, 2024

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see "Related Criteria"). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee’s assessment of the key rating factors is reflected in the Rating Component Scores above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see "Related Criteria").

Ratings List

Ratings List	
Ratings Affirmed	
Zagreb (City of)	
Issuer Credit Rating	BBB+/Positive/--