

2. Political risks in CESEE 2024-2025: Strategic outlook

BY MARCUS HOW²

- › **The European elections in June maintained the status quo, despite gains by nationalist and populist parties.**
- › **However, there is uncertainty ahead of the US presidential election, which is too close to call. If the Democratic candidate Kamala Harris wins, policy continuity is likely; if the Republican candidate Donald Trump triumphs, disruption may be expected in the areas of transatlantic trade and security.**
- › **Ukraine, Russia and the Western Balkans are particularly exposed to the policy changes that Trump is advocating. He would likely push for a peace agreement between Ukraine and Russia, to the detriment of the former.**
- › **Other regional developments to monitor include the fallout from the recent Austrian election and the outcome of upcoming elections in Romania and Bulgaria. In Slovakia, there is an increasing risk that the European Commission may suspend funding over its concerns about the rule of law and media freedom in that country.**

In 2024, the political risks across CESEE remain driven by the ongoing repercussions of Russia's invasion of Ukraine, while a wave of key elections – both already run and yet to be held – is only adding to the uncertainty surrounding policy stability.

The European elections witnessed an affirmation of the policy status quo in the EU, despite gains by nationalist, far-right and populist parties. The newly formed administration of European Commission President Ursula von der Leyen is re-committing itself to an agenda of strengthening the strategic autonomy of the bloc. There is likely to be an expansion of industrial policy that focuses on defence, renewable energy and technology, with the Commission moving beyond its traditional role of coordinating and complementing the activities of member states.

2.1. US ELECTIONS

Despite this, uncertainty remains elevated ahead of the US presidential elections. In July, the incumbent Democratic president, Joe Biden, agreed to terminate his re-election campaign and instead support the candidacy of his vice-president, Kamala Harris. This changed the dynamic of the election, which was tending heavily towards Biden's Republican challenger – the former president, Donald Trump. Nonetheless, the result will probably be very close.

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There will be repercussions for Europe irrespective of whether Harris or Trump wins the election; but those repercussions will differ significantly, depending on the outcome. However, there are two policy areas of particular importance for CESEE.

1. Trade

If Harris is elected, her administration will seek to maintain strong trade relations with the EU. Nevertheless, this policy area is by no means uncomplicated; not least as there are competition concerns arising from the generous subsidies provided by the Biden administration to reindustrialise large parts of the US economy as an element of the green transition. However, the overall trend is towards compromise and cooperation, as evidenced by the EU-US Critical Minerals Agreement of 2023, which coordinates green subsidy schemes so that they are mutually reinforcing.

If Trump is elected, his administration will not only maintain continuity with the protectionist industrial policy of Biden but will increase the scale of it. The impact of Trump's first administration was offset by those Republican moderates and internationalists who occupied key roles, but the new team assembled by Trump is dominated by isolationists.

Indeed, a Trump administration is likely to adopt a tougher stance on trade generally – which would also have an impact on the EU. Possible actions could include the imposition of sweeping tariffs of 10-20% on all imports (including those from the EU); or Section 301 of the US Trade Act could be deployed to take unilateral measures in response to activities that the administration views as harmful to American interests.

CESEE has very modest direct exposure to the US in terms of trade. In 2023, the US accounted for 1.35% of the region's exports and 1.19% of its imports. However, there is significant scope for indirect disruption. CESEE is far more dependent on trade than Western Europe, where domestic demand is stronger. And while its direct exposure to the US is limited, many economies in the region – especially those in the EU – supply the German manufacturing sector, which does export heavily to the US: indeed, Germany ranks fifth in the world in the volume of exports to the US.

The tariffs proposed by the Trump administration could also weaken the US dollar, impacting monetary policy. Trump has repeatedly stated that the president should participate in decisions taken by the Federal Reserve. Any major changes in this regard would impact global demand more generally, including in CESEE.

2. Security

If elected, Harris will maintain the Biden administration's commitment to NATO, which she has previously described as "iron." Specifically, she is likely to continue US support for NATO's 2030 initiative, which seeks to deepen political cooperation and consultation while broadening cooperation to increase resilience against non-conventional threats (e.g. cyber-attacks, climate change.) However, it is noteworthy that Harris has no unique interest in Europe, in which she is less personally invested than Biden, who already had extensive experience of the region.

Trump remains highly critical of NATO, to which he believes the US contributes disproportionately. At the very least, there will be increased pressure on NATO members to boost their defence spending –

something that would prove politically challenging in key states such as Germany. If a Trump administration does choose to challenge NATO, it is nonetheless very unlikely to initiate a formal departure from NATO, since such a move would require approval from the Senate; however, the organisation could be rendered obsolete.

For instance, Article 5 of the North Atlantic Treaty, which mandates mutual assistance by NATO allies in the event of an attack, can only be triggered collectively. Contributions are also left up to the discretion of member states. Additionally, a Trump administration could potentially opt to pull US troops out of NATO operations, such as those in Kosovo, placing the burden for maintaining security solely on the European allies.

Whoever wins – Harris or Trump – there will also be implications for two flashpoints of European security:

a. Ukraine and Russia

In 2024, the Russian war in Ukraine slowed to a stalemate that was tending in favour of the Russian military. Slow, costly, but significant gains were made in the Donbass region, eroding Ukrainian positions. An offensive was launched in Kharkiv region, and 90% of the electricity infrastructure of Ukraine that is not nuclear was incapacitated.

Ukraine regained some momentum for three reasons. First, after six months of legislative delay, it received much-needed military aid from the US, increasing its air defence radius. Second, it secured piecemeal support from the NATO partners to target military and energy assets in the Russian Federation with long-range missiles, buttressing its campaign of drone strikes. Third, it conducted a surprise offensive into the Kursk region of the Russian Federation, securing modest territory that it is defending, in order to divert Russian resources from the Donbass.

Nonetheless, the situation remains precarious for the Ukrainian Armed Forces, as Russian momentum in the Donbass is building. If Harris wins the election, she has committed to maintaining support for Ukraine, having been among its most vocal advocates in the Biden administration. In some areas, she could be bolder than Biden, whose support for Ukraine has wavered somewhat. Under such circumstances, it will be possible for Ukraine to sustain its defence, although war fatigue is increasing the likelihood that peace negotiations will be held within the next six months.

Trump has been vocal in his criticism of US policy towards Ukraine, pledging instead that he will end support and quickly forge a peace settlement – one that would likely be to the detriment not only of Ukraine, but also the wider CESEE region, given the security concerns of states such as Poland and the Baltics. Yet Trump is unpredictable, having backed down in his opposition to the military aid package passed by Congress earlier in the year. Similarly, his previous administration was hawkish in the substance of its Russian policy, contrasting with his dovish rhetoric.

The EU is increasingly aware of the potential for disruption in US policy towards Ukraine and Russia. For this reason, it has significantly stepped up its own support, the flagship initiative of which is the European Peace Facility (EPF). Meanwhile, it is preparing to raise EUR 35bn in loans to bridge the financing gap that Ukraine faces in 2025 – if necessary, without the US. This can be done without the

need for unanimity among member states, thereby circumventing the government of Hungary's Viktor Orbán, which blocked a previous proposal to use frozen Russian assets to fund support programmes.

Sanctions on Russia are a policy area of some uncertainty. If Harris is elected, her administration will keep the current sanctions regime in place. Currently, the Biden administration is pushing the EU to fix its sanctions package for 36 months (if not indefinitely), rather than having to renew it every six months. Hungarian opposition to this means that the requisite unanimity may not be achievable. In that case, member states will probably coordinate to impose sanctions at the national level.

b. Western Balkans

It has been the policy of the Biden administration in the Western Balkans to keep the region in the geopolitical orbit of the transatlantic community. Formally, this priority is locked in by EU membership prospects; but the substantive reforms in the region that the accession process requires are subordinate to the goal of ensuring stability. Local elites are thus tolerated, if not courted, because they are known quantities, whose acquiescence may be secured through the provision of incentives. The risk is that they would otherwise be susceptible to Russian influence, which has traditionally been brought to bear through the channels of energy, defence and the media.

This approach is not entirely one-sided: incentives are accompanied by the threat of sanctions being imposed on politicians and businesspeople suspected of corruption. Yet overall, the Biden administration has been transactional in its approach to the Western Balkans. The consequence of this is that incumbents there have been able to 'capture' state institutions. The approach is also not necessarily effective. For example, in September 2024 the US and Serbian governments signed an agreement on strategic cooperation in energy. At the same time, the Serbian government was conducting negotiations with its Russian counterpart on its gas supply agreement, which is due to expire in March 2025.

Harris has not indicated that she will discontinue current policy in any major way. She is reportedly considering replacing Biden's national security advisor, Jake Sullivan, with her own advisor, Phil Gordon, who has extensive experience of European affairs. Her prosecutorial background means that she is also interested in organised criminal networks. Nonetheless, any differences in approach will be modest.

If Trump is elected, it is likely that he will return to his previous policy in the region, which was similarly transactional, but not anchored in any particular geopolitical strategy. Since 2020, his family has acquired major real estate interests in Serbia and Albania. His former chief diplomat for the region, Richard Grenell, is very likely to be reappointed. Grenell would attempt to resurrect the 2020 Washington Agreement, which sought various forms of economic cooperation between Serbia and Kosovo, but which was not implemented. Grenell has very poor relations with Kosovan Prime Minister Albin Kurti, whose initial dismissal in 2020 he engineered.

The overall outlook for the Western Balkans is a continuation of the status quo, which emphasises short- to medium-term stability. This will serve to benefit the local incumbents, who have their own agendas. The approach of the EU has been similar to that of the US. In July, it struck a deal with Serbia for the supply of lithium. In August, the French government announced that it would provide the country with modern fighter jets and nuclear technology. Meanwhile, the enlargement process has stalled, despite notional progress.

2.2. REGIONAL DEVELOPMENTS

Beyond the US elections, there are other developments that may influence political risks in CESEE. The parliamentary elections held in Austria on 29 September saw the far-right Freedom Party (FPÖ) win a relative majority. The next 2-6 months will see negotiations over the formation of a coalition. The FPÖ's only viable partner is the centre-right People's Party (ÖVP), which came second. However, the ÖVP may be tempted to retain control of the chancellery through the formation of a grand coalition with the Social Democrats (SPÖ).

If the FPÖ does enter government, this is likely to have significant ramifications in multiple policy areas. The main focus of the party will be on immigration – an issue on which it overlaps significantly with the ÖVP. For example, it has pledged to restrict asylum to individuals who have not passed through safe third countries, and to introduce time limits on asylum status. Such measures could result in frontier controls and potentially have an impact on cross-border trade. The likelihood of such a scenario has increased since Germany imposed controls of its own, following the success of populist parties in state elections in Thuringia and Saxony.

The FPÖ is also likely to pose a challenge to consensus surrounding the Common Foreign and Security Policy in the EU, which hinges on unanimity – though the danger may be tempered by the ÖVP, which is more Euroatlanticist. Nevertheless, the FPÖ is opposed to the use of the European Peace Facility to provide Ukraine with military support, as well as humanitarian aid. It is likely to oppose enlargement, of which Austria is usually one of the main proponents. At the very least, it will probably reinforce the position of the ÖVP in blocking the full admission of Romania and Bulgaria to the Schengen area of free movement.

Another member state that is challenging the EU consensus is Slovakia. The coalition government led by the Smer party of Prime Minister Robert Fico could face punitive action by the EU for reforms that are regarded as undermining the rule of law. Currently, the European Commission is considering whether these reforms warrant the suspension of EUR 15bn in cohesion and recovery funds. That would have a significant impact on the Slovak economy, which is heavily dependent on investment and cannot rely on an independent monetary policy to manage shocks.

In December, Romania will hold elections to both chambers of parliament and for the presidency. The incumbent government, which is a grand coalition of the Social Democratic Party (PSD) and the National Liberal Party (PNL), is likely to be reconstituted. However, the race for the presidency – which commands a foreign policy remit, as well as considerable informal influence – is more unpredictable. If neither the PSD nor the PNL candidate wins, the stability of the grand coalition could be compromised.

That said, after the turmoil of 2016-2021, Romania has become a haven of relative stability in CESEE, and cohabitation between the government and the president is likely to be possible. Fiscal consolidation will be necessary to reduce the budget deficit, which stands at double the EU target. This is likely to be offset by a huge investment of EU funds, in particular in the energy sector; that would position Romania to become a major exporter of electricity and natural gas.

Elsewhere, in October, Bulgaria will hold its seventh parliamentary election since 2021. Despite this, there is currently no indication of any power constellation that could emerge to command a ruling majority and thus resolve the political stalemate. Thus, an eighth election is likely to be on the cards in spring 2025.