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Outlook for 2023 CEE region

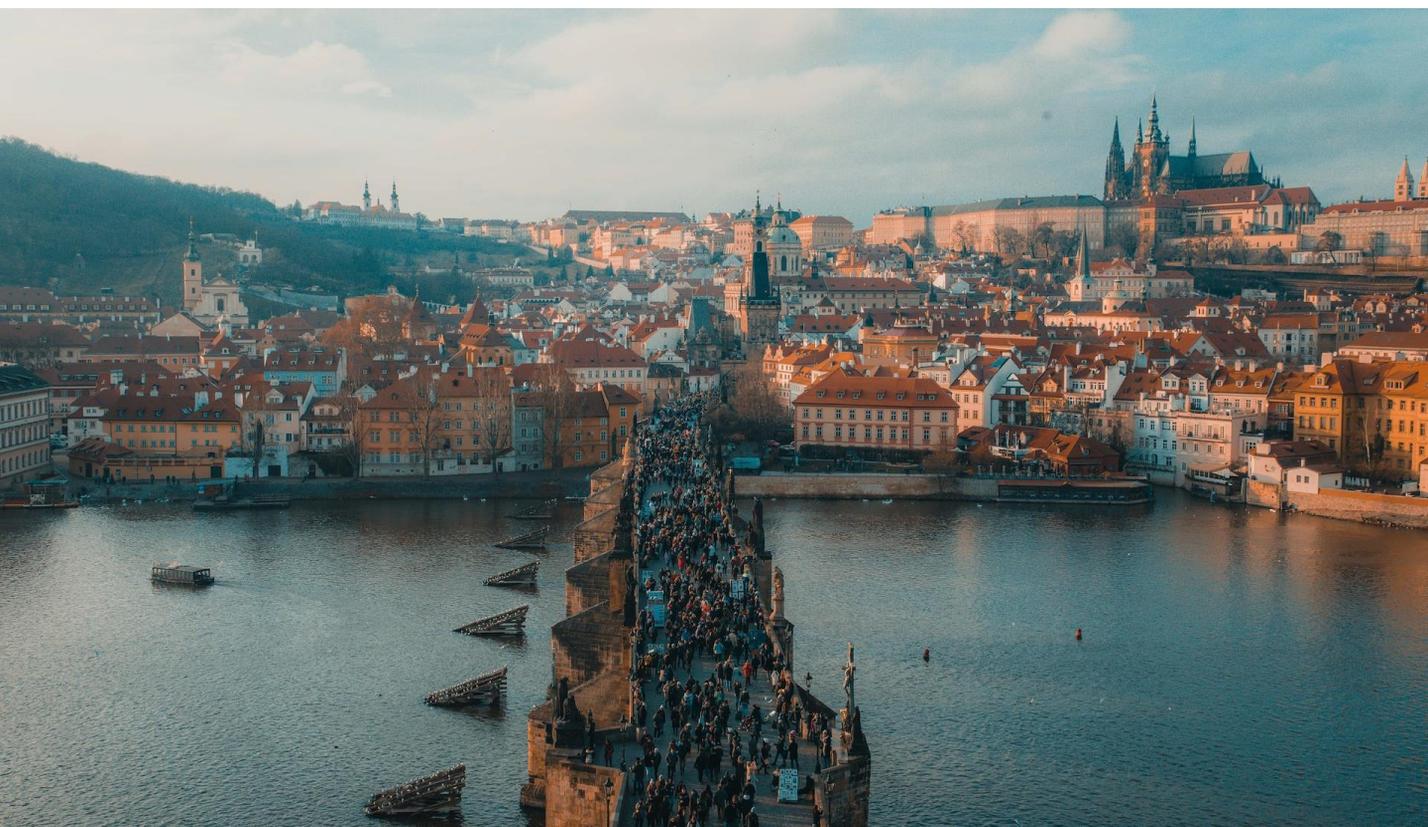
An overview of geopolitical
risks in 2023 in Central and
Eastern Europe

February 2023



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Grayling's viewpoint

An overview of geopolitical risks in 2023 in Central and Eastern Europe

The most evident geopolitical risk for the region is Russia's ongoing invasion of Ukraine. From the perspective of CEE, a Ukrainian victory is paramount to ensuring continued political stability in the region and CEE governments will certainly continue to coordinate with NATO allies, especially the US and Scandinavian members, Finland and Sweden. While a Ukrainian victory sooner rather than later would be preferred, so long as the trend toward an eventual Ukrainian victory is maintained in 2023, the risks to CEE will remain manageable.

That said, one cannot assume the support of western democracies for Ukraine will be unconditional. In other words, while Europe appears to have weathered the energy cost risks associated with weaning itself off Russian oil and natural gas supplies this winter, any extended challenges during winter 2023/2024 would represent a risk to continued support for Ukraine, especially if the tide of war turns against Ukraine. Ensuing fissures within the EU would represent a further political headwind for the region, which would only partly be mitigated by current US support for Ukraine.

While inflationary pressures are beginning to wane in CEE (apart from Hungary), tight physical markets for crude oil and especially diesel, as well as numerous commodities used in industrial processes (in addition to food prices), remain a relevant risk for CEE economies in 2023. Closely related is the increase in interest rates which the US Federal Reserve and in recent months, the European Central Bank, have both embarked upon.

Higher funding costs for governments and businesses will contribute to slowing domestic demand and therefore GDP

growth. Meanwhile, commodity and energy prices - which are materially higher compared to the pre-pandemic era - will put pressure on trade and therefore current account balances. This has the potential to generate additional currency depreciation risks for the economies in CEE that have not adopted the euro or do not have currency board arrangements in place, thus increasing the risk that inflation remains high.

Markedly slower growth is expected this year compared to 2022, but should these expectations prove too optimistic for the global economy and CEE, the political risks in the region will rise. Thus, even a scenario of lower-than-expected inflation may generate political risks if its genesis lies in slower than expected demand and thus GDP growth. Bulgaria, which has been characterised by political instability in recent years and faces another election in 2023, appears particularly at risk in this respect. A related issue, particularly for Hungary, is the risk of continued challenges in accessing its full EU funding quota due to EU concerns about illiberal democracy.

Finally, the US presidential election campaign will be fully underway by the end of 2023. The context in which this may develop as a risk to CEE is that there is increasing opinion poll evidence of Republican Party-affiliated voters tiring of US support for Ukraine. Although this is more of a risk for late 2024 and 2025, depending on whether the Republican Party provides the next US president (and what their stance on Ukraine is), we mention it as a factor certainly worthy of monitoring later in 2023.

CEE at a glance

Executive summary

Bulgaria

- In 2023, the Bulgarian government's key priorities will be to navigate through the expectations of different stakeholders in relation to the war in Ukraine, to ensure price stability and border security in order to be able to join the Eurozone and Schengen. This will be a challenge bearing in mind that a snap parliament election is scheduled for 2 April, while regular Municipal elections will be held in October.

Croatia

- 2022 was a very successful year for Croatia, with its entry into both Eurozone and Schengen area, and it is expected that there will be massive positive levers to push the economy in the long run.
- In 2023, it is expected that Andrej Plenkovic's government will aim to build advantage over their political opponents to secure easy wins in the super election year of 2024, when a general election, European Parliament elections and the presidential election are taking place.

Czechia

- The second half of 2022 belonged to the Presidency of the Council of the EU, and despite initial scepticism and low expectations, the Presidency can be assessed as successful.
- The most important political event of 2023 already took place in January with the presidential election, which brought decisive defeat for the former Prime Minister Andrej Babiš and placed an independent candidate, Petr Pavel, in the presidential office. The new

president's phone call to Taiwan shortly after the election symbolically ended the predominantly pro-China policy of outgoing President Miloš Zeman and demonstrate a shift towards the West.

- The political situation in the country should remain stable in 2023, with the current governing coalition holding a comfortable majority. There are no elections expected in 2023 and early 2024, which offers the government a unique chance to initiate systemic changes with a focus on consolidating public finances and reducing budget deficits.

Election timetable

- **CZECHIA:** Presidential elections held in January 2023
 - **BULGARIA:** Snap parliament election is scheduled for 2 April, while regular Municipal elections will be held in October
 - **SERBIA:** Although snap elections were already announced for spring 2024, only about two years after a previous snap election, the possibility that an even earlier election round will take place by the end of 2023 can't be ruled out
 - **SLOVAKIA:** Snap parliament election scheduled in September 2023
 - **POLAND:** Regular parliament election scheduled in autumn 2023
- # # #
- **UKRAINE:** The next Parliamentary elections in Ukraine were to take place in October 2023, but while martial law operates in the country, it will be impossible to hold elections

Hungary

- Although governing parties secured another supermajority in the Parliament in elections in April 2022, the Hungarian economy slowed down in the second half of the year before turning negative under the impact of increasing inflation, high energy prices, higher interest rates and deteriorating consumer and business confidence. In 2023, a real threat to the government could come from the direction of growing social discontent due to the economic slowdown and the international -especially EU-related - political stage.
- Despite EU institutions adopting the Partnership Agreement with Hungary and the Hungarian Recovery and Resilience Plan, the Hungarian government is still unable to access these EU funds due to concerns about the state of rule of law and corruption.

Poland

- Lack of EU funding to implement the National Recovery Plan meant Poland's GDP in 2022 was about EUR 12.7 billion lower than it would otherwise have been with the intake and successive distribution of the funds.
- As Poland is entering an election year, the United Right government will do everything in its power to put out all existing fires and prevent new ones from emerging. At the same time, the opposition struggles to find common ground and will probably opt not to run as one block of candidates, at least for the lower chamber. The latest polling suggests that the ruling coalition has a slight advantage over biggest opposition parties but would be unable to form the government

alone. If it decides to cooperate, the opposition stands a chance of claiming back power and open a brand-new chapter in Polish politics, introducing not only a different set of decision-makers figures, but also a completely different legislative agenda.

- Still, the major event of 2022 that fundamentally disrupted the geopolitical landscape, and transformed domestic economy and politics, is most certainly the war in Ukraine. The war in Ukraine will continue to take centre stage in 2023 and will resonate in almost all sectors of the economy. Security issues are going to be prioritised as the government wants to be perceived as a strong force, taking care of its citizens in difficult times.

Romania

- Romania's antagonist ruling coalition checked one year in administration in 2022 without major conflicts to threaten its existence. The Social Democrats (PSD) turned to be the leading partner in the coalition with the Liberals (PNL) and imposed nearly all major measures promoted by the Cabinet led by Liberal Prime Minister, Nicolae Ciucă.
- The political developments in 2023 will be influenced by two major events: 1) the Prime Minister rotation at the end of May, when current Liberal Prime Minister Nicolae Ciucă will leave office to be replaced by the Social Democrats' president, Marcel Ciolacu, and several key ministries will be exchanged; and 2) the European, local, general and presidential elections in 2024. With the elections in sight, PSD will need to consolidate - if not to increase further - its leadership position.

Serbia

- The foremost question for Serbia is its final stance in international relations, particularly regarding the Russian-Ukrainian conflict. Another challenge is the expectation from the international community that Serbia will finally reach a long-term resolution of its relationship with Kosovo by the end of the year.
- While some minor steps towards aligning with EU foreign politics were taken in 2022 and more are announced for 2023, it cannot be completely ruled out that pressure from pro-Russian and nationalist parties will triumph, leading the country to align completely with its eastern partners and move further from its EU integration and cooperation. Although it is believed that aligning with the EU's international affairs and reaching a resolution with Kosovo will result in improved economic conditions in 2023, it remains uncertain whether any substantial changes can occur without significant systemic improvements.

Slovakia

- 2022 was a very turbulent year in Slovakian politics. In September, the coalition liberal party Freedom and Solidarity (SaS) left the government and the ruling coalition lost the majority in the parliament. On 15 December, the government lost confidence in the parliament and President Zuzana Čaputová mandated Prime Minister Eduard

Heger to lead an interim government with restricted power until the snap elections scheduled for 30 September 2023.

- In 2023, we will see a major overhaul in the parliament, since ruling coalition parties have very low public support and it's likely they will lose the early elections significantly. Opposition parties (especially Voice – Social Democracy (Hlas-SD)) are on course to win the elections and form the new government. Probably, it will be a left-right government, so there is no expectation of abrupt changes in current policies. But the main challenge will be a state budget for 2024, because of the huge deficit in public finances in 2023.

Slovenia

- Slovenia saw 2022 as a super election year, with parliamentary, local, and presidential elections taking place over an eight-month timespan.
- This year is expected to be a year of reforms in Slovenia. As per Prime Minister Robert Golob's ambition, the government intends to handle all the challenges that have accumulated in the country over the past 30 years. Announced reforms include a tax reform, reforms of the public health system, housing and schooling systems, pensions reform, a reform of social transfers, and a reform of the public sector salary system, which could all potentially increase public expenditures.

SPECIAL FOCUS: UKRAINE

- Despite facing one of the worst years in decades, Ukrainian people and businesses are persevering and continuing their operations as much as possible. The biggest challenge for businesses, besides the dangers of war, is the power outages, leading some companies to reorganise or purchase industrial electricity generators.
- Some Ukrainian companies have even relocated their operations to the safer western part of the country or to neighbouring countries, such as Poland.
- The next parliamentary election in Ukraine was scheduled for 29 October 2023, but it is unlikely to be held while the war continues.

Economy indicators

	Forecast 2022 Inflation (%, yoy)	Forecast 2023 Inflation (%, yoy)	Forecast 2022 GDP growth (%, yoy)	Forecast 2023 GDP growth (%, yoy)
Bulgaria	12.8	7.4	3.1	1.1
Czechia	15.6	9.5	2.5	0.1
Croatia	10.1	6.5	6.0	1.0
Hungary	14.8	15.7	5.5	0.1
Poland	13.3	13.8	4.0	0.7
Romania	11.8	10.2	5.8	1.8
Slovenia	9.2	6.5	6.2	0.8
Slovakia	11.8	13.9	1.9	0.5
Serbia	11.9*	11.8*	2.7	2.4

Sources: *European Commission - Autumn 2022 Economic Forecast* / **Serbian Statistical Office / National Bank of Serbia*

- All CEE markets will see an economic slowdown in 2023 with estimated GDP growth rates from 0.1% in Czechia to 1.8% in Romania.
- Also, 2023 is expected to bring decreased inflation across CEE, except in Hungary. Although Prime Minister Viktor Orbán said that the goal is single-digit inflation by the end of 2023, according to the EC economic forecast the rate is expected to be 15.7% yoy.
- Moreover, Moody's Investors Service changed the outlook for Hungarian banking sector from stable to negative. Similarly, Fitch has revised the outlook on Hungary's Long-Term Foreign-Currency Issuer Default Rating to Negative from Stable and affirmed it at 'BBB'.
- On average, CEE countries recorded higher inflation rates in 2022 compared to other Western European peers, and this situation may continue in 2023 as well. Recorded inflation rates across the continent evoke bad memories from the 1980s, and the CEE region is probably additionally threatened by declining consumer purchasing power and shortages of critical raw materials.

Bulgaria

2022 in review

- A short-lived cabinet in the first half of 2022 created conditions that boosted inflation to levels seven points above the EU average. Political instability in second half of the year prevented critical legislation to be passed. As a result, **Bulgaria may miss its chance to join the Eurozone on 1 January 2024 as planned.**
 - Sofia Airport failed to cover basic security and safety standards at a recent pen test conducted by EC officials. As a result, the vote at the end of 2022 on joining Schengen, did not go in favour of Bulgaria. However, **several stakeholders now claim that by the end of 2023 all issues will be resolved and by 1 January 2024 Bulgaria may join the Schengen area treaty.**
 - The political crisis which started in 2021 is still ongoing, with mainstream parties unable to negotiate a stable cabinet, so President Rumen Radev is practically governing the country most of the time.
- part of a coalition cabinet for the foreseeable future.
 - Nationalists are on the rise and may become an important political factor if the crisis continues.
 - The war in Ukraine exacerbates the situation and anti-European propaganda is now more efficient. For the first time in three decades, EU pessimists prevail on important issues such as joining the Eurozone.
 - **The political turmoil threatens to derail all the strategic goals of the Bulgarian government.** The war in Ukraine, the rise of the pro-Russian nationalists as well as the soaring inflation across Europe only add to the complexity of the situation. That is why **only a stable cabinet with a wide majority in the House can navigate through these overlapping crises.**

Political outlook

- **Four Parliamentary votes proved to be inconclusive. A fifth vote is upcoming on 2 April with no better prospects likely for a stable cabinet.**
- Bulgarian citizens are now split on many issues and the overlapping differences create schisms in society that run deep and cannot be bridged by a simple vote. In the conservative corner, competing parties try to reach a consensus on what is important for the nation and may be able to produce a relatively stable coalition, while the liberals seem reluctant to negotiate and be



Croatia

2022 in review

- 2022 was a very successful year for Croatia and the current Government run by the Prime Minister Andrej Plenkovic. The **adoption of euro and entry in Schengen** will be massive positive levers to push the Croatian economy in the long run. This way, Croatia joined an exclusive list of 15 countries that are members of NATO, the Eurozone and Schengen. On top of that, through the finalisation of the Pelješac bridge, a project which was funded through the EU, Croatia also became territorially connected. The 2.4km long bridge will allow easier transport of goods and people to south Dalmatia (Dubrovnik) and is a source of national pride for Croatians.
- Throughout the 2022, Russian aggression over Ukraine was felt economically socially, and also physically with an unidentified pilotless military aircraft crashing in Zagreb, the Croatian capital. The aircraft crashed near one of the biggest student dorms in Croatia causing damage to nearby vehicles and only by pure luck was nobody injured. **The situation in Ukraine was the ongoing topic between the Government and the President of the Croatian Republic, where at times, President Zoran Milanović expressed completely opposite views from the Government, which strongly supports Ukraine's efforts for freedom.** Croatia is one of the few countries in EU that has recent war experience and fought for its independence during the early 1990s.
- The Government was not afraid to tackle inflation with market interventions into energy prices (gas, electricity, and petroleum) or by limiting essential food prices. It kept

social order and, despite key ministers walking away, preserved the ruling position. **The departure of Zdravko Maric, Minister of Finance, was met with many raised eyebrows and up until this day, the real reason of his departure is unknown.** He was well respected by the business economy and was one of the most component ministers of finance in Croatian history.

Political outlook

Stable government expected to complete its term

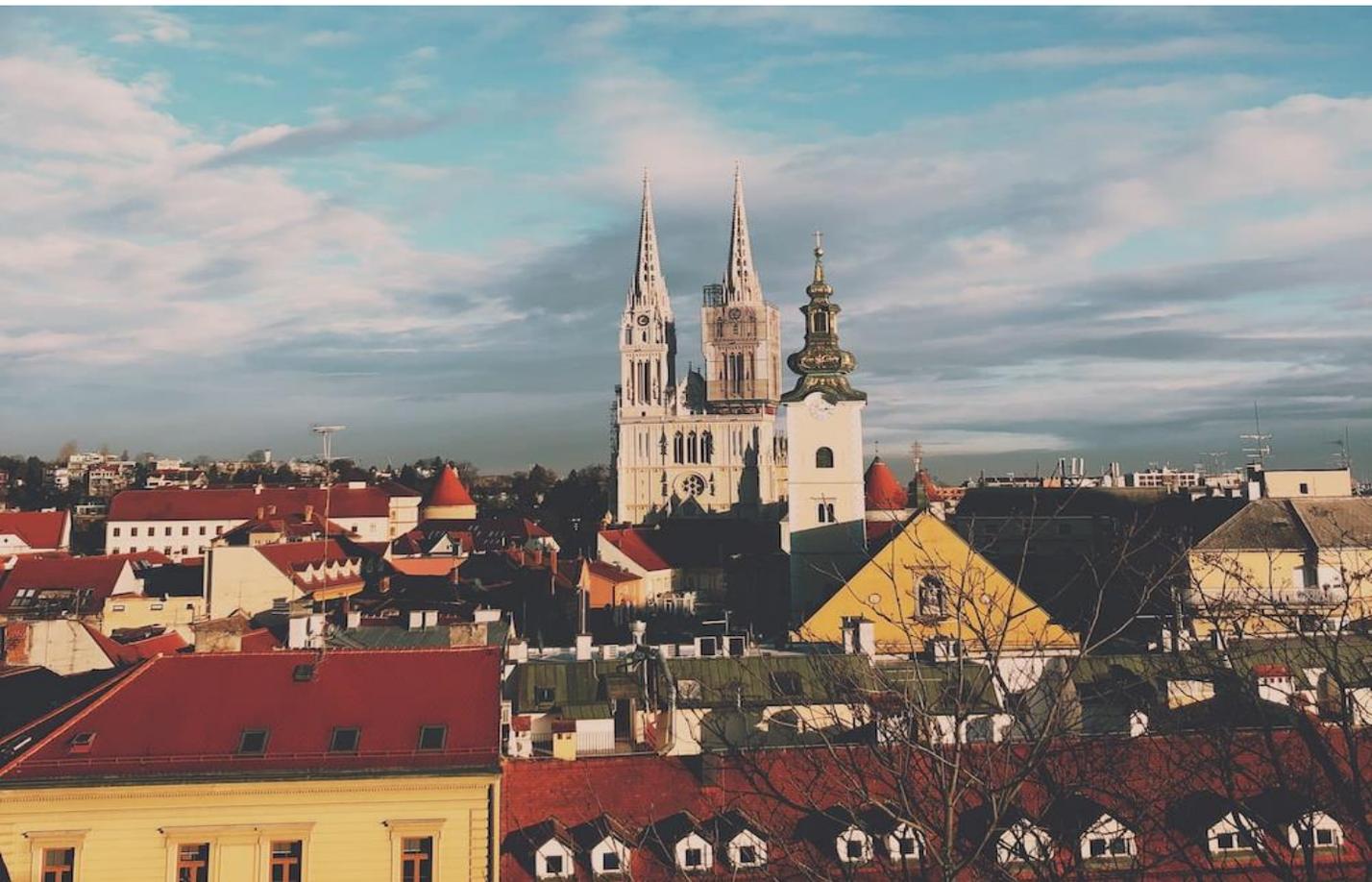
- Despite continuous turnover of the ministers in the Andrej Plenkovic's government in the past three years (and four years before that), the Prime Minister is showing no signs of weakness to his political opponents.
- Mr Plenkovic has the full support of the ruling Croatian Democratic Union (HDZ) and aims to win a third consecutive governmental term. HDZ benefits from a weak opposition that could otherwise challenge it. Both the left and centre has been dispersed and with the second biggest party, Social Democratic Party losing public support daily **we don't see a situation where there would be preliminary general election.**
- On the other hand, the glooming chances of a political scandal arising is also a possibility which could change this position. So far, few 'skeletons in the closet' did not harm the ruling party with the last being a high ranking HDZ member embezzling almost EUR 133 million from the state-owned energy company INA (INA is majority owned by the Hungarian MOL 49.08%, Croatia owns 44.84%).

- Both during the pandemic and in 2022 during the energy crisis, the Government was very supportive of the general public and the business sector, providing financial aid. The most recent aid was the autumn package to tackle inflation (adopted in September 2022), which introduced energy subventions and expires on 31 March 2023. The Prime Minister Plenkovic announced that the Government is assembling the finance team to assess the capacity of any future government's measures against rising prices.
- Croatia is one of the biggest beneficiaries of the Recovery and Resilience Facility and the Government will continue with the reforms listed in the National Recovery and Resilience Plan to secure EU funding. One of the biggest NRRP projects for 2023-2024 is the digitisation of motorway tolling system.

Preparing for the super election year

Priorities in 2023

- Again, **inflation** will be one of the key topics in 2023 as forecasts show the gradual slow-down of inflation. While monetary policy is out of the equation, the Government will look to adopt measures that will alleviate the inflation pressure, at least for the vulnerable social categories.
- Barring any surprises, the 2024 will see three different elections in Croatia: 1) general election 2) presidential election and 3) EU election. Understandably, the ruling HDZ holds the best position to sweep all three elections as the opposition is continuously failing to rally their electorate under one banner.
- **HDZ is expected to play it safe in 2023** without making any controversial decisions and changing laws that could create friction.



Czechia

2022 in review

Presidency of the EU Council

- Czechia has held its second Presidency of the Council of the EU, which undoubtedly was the major event for the Czech Government in 2022. Despite the initially low ambitions, when the main goal was to survive the Presidency without any major scandal, the **Czech Presidency can be evaluated as relatively successful**, especially in view of the complicated period when the agenda was determined mainly by energy and other issues related to the Russian invasion of Ukraine.
- Given the good international response, especially in the EU institutions, **Czechia has managed to at least partially improve its image as a troublemaker and somewhat lazy EU member**. The coming months will show whether Czech diplomats and politicians will be able to further exploit the successful presidency and possibly strengthen their negotiating power within the EU and their presence in the European institutions, which could reflect on the promotion of Czech priorities in the future, including in the energy sector. With the end of the presidency, the Government will now have more space to focus on domestic issues as well, which were partly neglected during the presidency.

Political outlook

Prospects of stable political development in 2023

- In the parliamentary elections in October 2021, the current governing coalition won a comfortable majority of 108/200 votes, and although it includes a wide range of political parties (conservative, liberal-conservative and progressive-liberal),

the government has so far shown considerable stability by the standards of Czech politics. So far, there have been no major disputes within the coalition. The representatives of the ruling parties are undoubtedly aware that snap elections would very likely mean the return of Andrej Babiš to power, so the current ruling parties have a strong incentive to avoid this situation. It **can therefore be assumed that the composition of the Czech government will remain without major changes in 2023**.

- Additionally, now comes a rather rare period for Czechia. For almost a year and a half there should be no elections at all. The last time such a situation occurred was in 2015. The next elections that Czech citizens will participate in will be those for the European Parliament in 2024. For the current government, this means a rather unique chance to initiate significant systemic changes. **It is already clear that the government will want to focus particularly on consolidating public finances and gradually reducing the huge budget deficits** that have accumulated in recent years. Reducing the state debt, however, means adopting unpopular measures that may sway more voters to populist groups such as ANO and SPD in the future.
- In the first quarter of 2023, the Government will present an updated Program Statement outlining the Government's objectives and activities for the entire election term. The government coalition has been forced to make this change due to the impact of the war in Ukraine and the energy crisis on the national economy. Due to this fact, the government will abandon its pre-election promises not to raise taxes.



Presidential election

- **The most important political event of 2023 already took place in January with the presidential election, which brought a decisive defeat for the former Prime Minister Andrej Babiš and placed an independent candidate, Petr Pavel, in the presidential office.**
- Immediately after his election and even before his official appointment as President, Petr Pavel actively embarked on foreign policy. His phone call with the President of Taiwan shortly after the election symbolically **ended the predominantly pro-China policy of outgoing President Miloš Zeman and shift towards the West.**
- After years of somewhat inconsistent foreign policy, when there was often no unified position between the President, the Prime Minister, and the Foreign Minister on key issues, we can expect that the highest constitutional officials will now speak with one voice as there is consensus between the government and the new President on the foreign policy direction of the country. This will make Czechia much more predictable and easier to understand for its EU and NATO partners, which was certainly not the case in previous years. In the wake of a successful EU Presidency, Petr Pavel can attract more attention towards the country and strengthen its position in the EU.

Hungary

2022 in review

Electoral triumph of the government, but ongoing struggle for EU money

- After **governing parties secured another supermajority in the Parliament in April 2022** (with a record-high 54.1% of the votes against the united opposition list's 34%, which is a spectacular and larger-than-expected political triumph), we have witnessed the **resurgence of the so-called "central field of power" in Hungarian party politics**, while opposition voters became demoralised, and their former parties became (again) fragmented and weak.
- Although the electoral support of government parties has declined from 39% of the eligible voting population total in October 2022 to 32% in December 2022, the significant level of difference has increased the undecided voters (from 23% to 30%), rather than fragmented opposition parties (together around the remaining third of eligible voters).
- **Although EU institutions adopted the Partnership Agreement with Hungary**, which is necessary for access to resources of the 2021–2027 multi-annual EU budget (cohesion funds), **and the Hungarian Recovery and Resilience Plan**, which is necessary for access to Recovery and Resilience Fund (RRF) at the end of the 2022, **the government is still unable to access these EU funds due to concerns about the state of rule of law and corruption.**



Political outlook

2023 as a particularly challenging year for the government

- We expect **new rounds of negotiations between the EU and the Hungarian government in 2023**, starting in March/April, in which the threat of further withholding of EU funds from the EU side, and pressure from the Hungarian government with tactical vetoes (such as in late 2022) are expected to continue. The intensity of these will depend partly on external circumstances, most importantly the Ukraine-Russia war and the economic recession. Nevertheless, **we continue to expect a game of chicken ending in political compromises** and the disbursement of part of the funds, starting in second quarter at the earliest.
- The government's room for manoeuvre will be limited in autumn, which will already be the start of the campaign mode of domestic politics, as there will be European Parliament elections and municipal elections in spring 2024. Therefore, **the end of budgetary rigour with austerity and unorthodox economic measures, and the (re-)start of welfare transfers are expected in autumn 2023**, especially if the government will have at least partial access to EU funds.
- **2023 is likely to be accompanied by a rhetorically more anti-Western and anti-Brussels discourse**, which is already used as a justification of the worsening economic situation and the unpopular measures of the government. Indeed, blaming Brussels for domestic problems to channel societal fears and anger was again a key strategy of the government in the second half of 2022. Therefore, it is likely that the EU will remain the government's key target.

Poland

2022 in review

- 2022 began with the entry into force of the ruling party's (Law and Justice) **flagship “New Polish Deal” political programme**, which included a comprehensive tax reform. Changes impacted almost all taxpayers, introducing modifications in the PIT and numerous tax changes for businesses. **The project was supposed to be a great success for the Prime Minister and his team, but in the end, it completely backfired.** The bill was passed at an alarmingly fast pace for a reform of this magnitude. The legislative text was full of legal errors, loopholes, and ambiguous provisions. The government failed to properly inform the public as to the actual effect of this reform on salaries and system of tax deductions. When the new provisions entered into force, it turned out that, a great number of professional and social groups (such as teachers or pensioners), especially the middle class, received significantly lower incomes, which was met with public backlash.
- At the same time, the government was in the midst of the ongoing conflict with the European Commission. Even though Poland's National Recovery Plan (KPO) was approved in July 2022, **the government has failed to reach an agreement with the European Commission** to unblock funding - €36 billion in grants and low-interest loans. **The discord centers around the rule of law and implementation of required milestones. Even though, Poland has made some progress and fulfilled majority of milestones, the most problematic reforms remain ongoing.**

However, most recently, we can see a major shift in Poland's position, and it seems a compromise is within reach. Making peace with the European Commission and gaining access to EU funding has **become a priority for the ruling party in 2023.**

Still the major 2022 event that fundamentally disrupted the geo-political landscape, and transformed domestic economy and politics, is most certainly the war in Ukraine. Since 24 February 2022, more than 9.5 million refugees from Ukraine have crossed the Polish border. In the first days of the war, there was an increased concern among Poles about fuel supplies, resulting in queues at petrol stations and temporary increases of fuel prices. Similarly, some Poles feared about their finances, making them flood ATMs to withdraw cash.

Thanks to special legislation passed on 12 March 2022, **Ukrainian refugees obtained residence permits and right to work for 18 months, as well as access to healthcare and social benefits.** As a result of the refugee influx, it was possible to partially fill the gaps in the Polish labour market and stabilize the economic situation.

Since the war in Ukraine started, the international image of Poland has noticeably improved. This is mostly attributed to active diplomatic efforts that Polish officials have been making to garner support for Ukraine. Not only has Poland received the majority of refugees, but it has also been publicly urging the EU to impose the toughest possible sanctions on Russia.

The **war in Ukraine will continue to take centre stage in 2023** and will resonate in almost all sectors of the economy. Security issues are going to be prioritised as the government wants to be perceived as a strong force, taking care of its citizens in difficult times.

Political outlook

- Law and Justice party together with its acolytes forming the national-conservative United Right coalition has been in power since 2015. However, **maintaining a stable majority in Parliament has been quite challenging for the government.**
- The vote for the next four-year term of the Parliament will take place as scheduled in **autumn of 2023**. This means **that from the beginning of 2023, political parties will be in full campaign mode.** The policy focus will most likely be the economy, raging inflation and energy prices. In addition, we can expect the ruling camp to continue distract polarised voters with its anti-minority, anti-European and anti-German narrative. The latter seems to be already taking centre stage and will definitely come back as the campaign unfolds. Law and Justice will also try to divert attention from its own shortcomings and point the finger at the opposition. The new initiative to set-up a committee to investigate Poland's energy policy in the years 2007-15, which was governed by current opposition, seems to be a preview of what to expect in the coming months.
- **As far as the result is concerned it will be difficult to predict and will probably be a close call.** On one hand, the governing party continues to fall in polls as its popularity is consecutively damaged by inflation and resulting spikes in prices of food, energy, and fuel prices. On the other hand, due to strong polarisation, the current authorities still enjoy a fairly broad support, especially from its core electorate. On the other side is a **still much-divided opposition, struggling to find a common agenda capable of uniting its voters** and attracting those who normally refrain from voting. **There has been a**

vigorous debate as to whether Poland's opposition should join forces and contest the election as one single list.

- According to the latest polls, **the ruling party has a slight advantage over biggest opposition parties but would be unable to form the government alone.** Combined opposition, on the other hand, gathers enough support to gain a majority. **The tide may turn at any moment and tip the balance in favour of change.** This would be a political game-changer, with new political figures and decision-makers entering the scene.

Government to continue juggling pro- and counter-inflation economic measures

- Polish government conducts a **“soft landing” economic policy** that aims at lowering inflation, but at the same time strives to prevent the economy from cooling down and falling into recession, which could increase unemployment and cause bankruptcies. For this reason, the government continues to **take actions that minimize the social costs of the energy and living costs crises.**
- One of them is 0% VAT on food staples. Such a solution was already part of the so-called **“anti-inflation shield”**, which in February 2022 scrapped VAT on food, gas, and fertilisers. However, because of EU rules, only VAT relief on food remained throughout 2023 and a new measure to cap gas prices has been introduced.
- In 2023, similar **pro-inflation policies** – like the 14th pension and extension of the credit vacations – are expected to stay, slowing down the effect of tightening of the monetary policy.

Romania

2022 in review

Our year together: Romania's arranged marriage goes relatively well

- **Romania's antagonist ruling coalition completed one year in administration in 2022 without major conflicts to threaten its existence.** The two former foes turned partners, the leftist Social Democratic Party (PSD) and the centre-right National Liberal Party (PNL), plus their junior partner, the ethnic Hungarians' party UDMR, benefited fully from their 65% majority in the Parliament to mute the opposition and render it useless. The arguments between PSD and PNL were the only ones grabbing headlines but even those were more marriage quarrels than serious political fights, thus so far, no major shake-up in the coalition has been registered.
- The PSD turned to be the leading partner in the arranged coalition with PNL, brokered by Romanian President Klaus Iohannis in the autumn of 2021. Benefiting from a powerful propaganda machine, disciplined leaders and a structured political agenda, **the Social Democrats imposed nearly all major measures promoted last year by the Cabinet led by Liberal Prime Minister Nicolae Ciucă:** a review of taxes, with tougher conditions for SMEs and part-time labour contracts; changes in the way tax exemptions were computed; VAT changes; and tax rises, including a hike in dividend tax and higher taxes for alcohol, soft drinks, tobacco and gambling. **On the populist side, PSD advocated and implemented a rise of the minimum gross salary,** which reached approximately €610 per month as of 1 January 2023, **and increased pensions** by 12.5%. When the government stumbled on the

measures aimed at alleviating the impact of high energy prices, PSD leaders were quick to point the finger on PNL's Energy Minister Virgil Popescu. The country's failure to join the border-free Schengen zone, following Austria's veto, was again directed, albeit muffled, towards the Liberal Interior Minister and the country's President Iohannis, a former Liberal.

- PNL remained unable to overcome its internal struggles and had no real Liberal initiatives to brag about last year. Its leader, the retired Army general-turned-politician and now Prime Minister, Nicolae Ciucă, went for peace at all costs in the ruling coalition, an approach that might cost its party dearly in the upcoming elections. The opinion polls, although unreliable and still far from the electoral mood, show PNL declining much below 20%, while PSD flies high at 35%.





Political outlook

Question of the year: how much further left can Romania turn?

- **With Romania facing four rounds of elections in 2024 – European, local, general, and presidential, political parties will struggle hard for positioning this year. The Social Democrats (PSD) need to conserve, if not increase further, their leadership position.** In the 2024 elections, it might be difficult for PSD to get a majority by itself or just with the current junior partner, the ethnic Hungarians' party UDMR, but it needs to make sure that in a renewed coalition with the Liberals (PNL) will grab all the major levers of administration.
- It's a difficult journey for PSD, given the fact that its leader, Marcel Ciolacu, Speaker of the Chamber of Deputies, will take over the Cabinet's helm in May, according to the rotation agreement signed with PNL at the inception of the current coalition. More than one year leading the government is enough to erode any political leader, especially with recession clouds looming above. And there is more at stake for Ciolacu, who will decide next year his political future. With his party running high, the Prime Minister's seat is already nailed down for him, but the alternative could be more lucrative: Ciolacu might go for Romania's Presidency, a position that doesn't formally have

many executive powers but has plenty of influence, especially if the President is a connected maverick player. More importantly, the presidency is for five years, or very likely ten with two terms, while the Prime Minister's seat is prone to the economic performance of his Cabinet.

- Until then, the show begins this year, with the rotation of the Prime Minister's seat at the end of May, which is supposed to be accompanied by the rotation of several key ministries: Finance, Justice, Transports and EU Funds. PSD would very much like to keep things as they are, continuing at Finance and Transport, but this might be too much to swallow for the pacifist Liberals. The PSD also threw out several economic measures, including a so-called "solidarity tax" seeking to take 1% of the turnover of major corporations and a planned decrease of labour taxation. So far, PNL has strongly opposed the tax, but it remains to be seen if it doesn't mellow later given the badly needed budget revenue in pre-election year.
- **What's for sure is that opposition has little chance of getting a seat in the next government.** The Alliance for the Unity of Romanians (AUR), a nationalistic, xenophobic party is rising in polls, at close to 15%, but there is no way it would be accepted to be part of any ruling coalition that wants to maintain a European face. The other opposition party, Save Romania Union (USR), once touted as the hope of young and anti-system voters, fell into the shadows after it broke the centre-right ruling coalition that emerged after the 2020 elections. Their rather childish and unreliable behaviour from the past would very likely prevents other parties to seek a partnership in the future.

Serbia

2022 in review

Election, election, election

- After announcing that the government formed in 2020 will only endure for roughly a year and a half, Serbian President Aleksandar Vucic called for a snap election to be held in April 2022. Once again, in mid-2022, before the formation of the new government, President Vucic said that its term is also limited to 18 months, which means that the next election in Serbia may be expected in early 2024, if not by the end of 2023.
- The Serbian Progressive Party (SNS), a populist big-tent party led by President Vucic won 44.3% of seats in the National Parliament in April's election, which was their lowest result in a number of years. However, the SNS once more formed a powerful government in coalition with their long-time ally, the Socialist Party of Serbia (SPS), as well as other smaller supporting parties. As announced by the old-new Prime Minister Ana Brnabić, the new government "will continue its European path, while continuing the fight for Kosovo and Metohija, and strengthening of partnership with all partners, both in the East and in the West."
- Judging by the names of appointed ministers, the new government appears to have been formed in an attempt to appease all of Serbia's international partners, both western and eastern. Yet, none of the ministers are expected to be strong political actors, but all of them will, instead, just serve as agents of the President Vucic and the SNS, without their own independent voices.

Another year in limbo

- "Despite the increased polarisation on the international stage in 2022, Serbia appears to have maintained its neutral stance in foreign policy throughout the year. Although some Western partners understand Serbia's position and its dependence on Russia, especially regarding energy supply, it remains to be seen what the long-term cost of this stance will be and for how long it can be sustained.
- Kosovo was probably the most mentioned word in Serbian politics in 2022, as it had been in previous years. Mutual verbal attacks between Serbian and Kosovo sides additionally fuelled tensions, leading to desertion of Serbian representatives from Kosovo institutions, the establishment of barricades, and sporadic firearm assaults by the end of the year. At the same time, negotiations between the two countries under the auspices of European countries and the USA continued throughout the year, resulting in some minor agreements. However, no significant progress was made in 2022 on this issue, while it seems that the deadline for reaching some kind of agreement is rapidly approaching in 2023.
- While worrying about international and regional affairs, Serbian society seems to continue its decline in terms of democracy, rule of law, and corruption prevention, along with worsened economic conditions caused both by international circumstances and local systematic issues. Although environmental protests in early 2022 appeared to be an opportunity for Serbian citizens to have more influence in politics, it now seems that the fulfilment of protesters' demands was just part of an election campaign.

Political outlook

Key political issues remain unchanged

- Relations with Kosovo, stance towards the Russian-Ukrainian conflict, and the country's relationship with major international powers like the USA, EU, Russia, China, etc. will likely continue to be key political and public topics in 2023. After years of nationalist and pro-Russian and pro-Chinese propaganda in local media influenced by the ruling establishment and its partners, it may seem like an impossible task for President Vucic and his party to make any further concrete steps towards reaching a long-term agreement with Kosovo or imposing sanctions against Russia. However, the beginning of 2023 brought some changes in the language used by state officials and pro-government media, which could indicate that Serbia wants to/will have to make a final decision and align itself with European foreign policy. Although there may be some resistance to taking a pro-Western approach in the following months, it is uncertain whether opponents will have any real power to change the ruling party's decisions.
- While Serbia may eventually make some significant decisions on the international stage (although this process will likely be prolonged as much as possible), any substantial changes in internal affairs, such as enhancing democracy, media, and political freedoms, upholding the rule of law, or combatting corruption, are even harder to anticipate. Despite the fact that there is a great deal of opposition to the SNS's control and that this could cause social upheaval, the opposition is weak and has a poor track record of gaining the public's trust.

EU accession and regulatory changes

- The country's EU accession process

influences almost all parts of Serbian everyday life, including laws regulating business and other relevant topics. This requires eventual alignment of regulations and practices in all business areas, including foreign payments, competition, digital services, environment, energy, as well as judicial and institutional reforms. However, it is currently unclear what the dynamics of these changes will be and how quickly the country will move towards EU accession.

Economy endangered by politics

- According to announcements made by Serbian President Vucic, Serbia may face severe sanctions if it fails to reach an agreement with Kosovo in the near future. This could lead to a decrease in economic activity, mass layoffs, and a decline in exports, among other negative consequences. Although this outcome is not likely, any failure by Serbia to align its foreign policy with the expectations of the EU could result in "silent sanctions", which would reduce foreign investment and ultimately lead to a long-term deterioration of economic conditions. However, aligning with the expectations of Western countries (the EU and the USA) does not guarantee an improvement in economic conditions for Serbia, meaning that the country will eventually have to rely on its own efforts for further development and prosperity.



Slovakia

2022 in review

The political turmoil and the fall of the government

- **2022 was a very turbulent year in Slovakian politics.** In September, the coalition liberal Freedom and Solidarity party (SaS) left the government, and the ruling coalition lost the majority in parliament. The Prime Minister Eduard Heger (Ordinary People and Independent Personalities conservative party OĽaNO) appointed four new Ministers – Foreign Affairs, Justice, Economy, and Education. The minority government has successfully passed several laws with support of independent parliament members but was unable to govern smoothly. It ended in the no-confidence motion in parliament during December 2022.
- **On 15 December, the Government lost confidence in the parliament and President Zuzana Čaputová took some responsibilities and mandated Prime Minister Eduard Heger to lead an interim government with restricted power** until the early elections. In January 2023, the change of Constitution was adopted in the parliament, and it opened a way for early elections, that will be held in September.
- During the pandemic years and in 2022 during the energy crisis, the Government was supportive but very unpredictable regarding the actions to the public and the business sector. Financial aid was generous, but constantly changing, so the overall perception is more negative.

Political outlook

Snap elections

- The ruling coalition parties face a significant loss of public support since the last elections, so **we can expect a completely new government to come.** It means the changes will happen almost in all stakeholders' state institutions.
- **There are two probable outcomes regarding the formation of a new coalition.** Either there will be left-right (centrist) coalition led by Voice – Social Democracy party (Hlas-SD), or the leftist coalition led by Direction – Slovak Social Democracy (Smer). The first one would be pro-European and pro-democratic one, the second one could be more dangerous for the next development in several areas, especially foreign policy, civic rights and liberties, business orientation.
- The key parties to watch in the forthcoming period are:
 - Hlas-SD** is a new party formed by former Prime Minister Peter Pellegrini who split from Smer-SD after the last elections with some other parliament members. Hlas-SD is leading the polls on a long-term basis, and it will probably win the snap election. Their policies are not left nor right and we could say they are more likely to align well with policies coming from Brussels.
 - Smer-SD**, after losing significant group of members of the parliament headed by former Prime Minister Peter Pellegrini, dropped below 10% in the polls. They managed to regain support of voters and now has consistently over 15% support. Their coalition potential is low, especially due to extreme positions on foreign policy (more pro-Russian stance) and hate speech led by its leader, Robert Fico.

Sme rodina is only party in the current government that was able to hold its support during the entire period. Also, it is a party that has a very strong coalition potential toward both sides of political spectrum. It is almost certain that they will be a part of the next government since they have good relations with opposition parties Hlas-SD and Smer-SD. It is a populist party, but it is also strongly linked to some businesses, so it is difficult to define their policies.

Progressive Slovakia (PS)– In the last parliamentary elections PS created coalition with party Spolu. However, due to the higher election threshold for coalitions, they failed to get into parliament. Since September 2022 they are getting higher political support and most likely will be successful in the upcoming parliamentary elections. On the other hand, its coalition potential remains questionable.

Economy measures

- **Government measures on energy prices will be effective in preventing a decline in citizens' living standards in 2023.** The government action is stopping what would otherwise be a significant increase in living costs for households, hence they are likely to avert a contraction of the economy and of households' real incomes and their purchasing power next year.
- **If energy spot prices remain at high levels, households can expect their energy bills to rise significantly by 2025.** Inflation may therefore remain elevated for an extended period and become anchored in the expectations of people and firms. At the same time, the public finances are in a state that precludes the government from subsidising the large differences between spot and consumer energy prices over the long term.



Slovenia

2022 in review

- Slovenia saw **2022 as a super election year**, with parliamentary, local, and presidential elections taking place over an eight-month timespan. Parliamentary and presidential elections brought **big changes**, as the new government is led by Robert Golob, a political newcomer, ex-CEO of regional energy company Gen-l. Also, for the first time in the short 30-year history of Slovenia, the country has women at the head of two branches of power; parliament is headed by former judge Urška Klakočar Zupančič, while in December lawyer Nataša Pirc Musar became the new President of Slovenia.
- The Golob government was immediately faced with handling the **energy crisis**, provoked by the war in Ukraine, which they are **handling with measures to limit the growth of energy prices and with energy supplements for citizens and companies**. A mild winter was of help to the nation as prices of solid fuels have risen by 97.5% in the last year, electricity by 100%. As a result of limiting the prices of energy products, the largest oil trader in the country, Petrol, announced a lawsuit against the state, which is indirectly the largest owner of the company.

Political outlook

2023 announced to be the year of reforms for Slovenia

- A newly established Ministry of the Environment, Climate and Energy will be tasked with drawing up measures to prevent an energy crisis happening ever again and will also be working on climate change mitigation and adaptation. The new super ministry is part of a **cabinet reshuffle** that Prime Minister Golob announced

immediately after taking power. The new government has 20 ministries, of which one without portfolio. Three ministers in the governmental team are new, while the briefs of another six have been reshuffled. Two former governmental offices without portfolio, for digital transformation and cohesion policy, have been elevated to ministries. Prime Minister Golob stated that the three new ministries will be the engines of **three important reforms in a year that his government has designated as a year of reforms that are to transform the country**.

- Prime Minister Robert Golob has announced a **long list of reforms for 2023, which includes tax reform, reforms of the public health system, housing and schooling systems, pension reform, and reform of social transfers and of the housing system**, which could all potentially increase public expenditures.
- Members of the coalition are to finetune major reforms at coalition summits, that are to take place by the end of March.
- For now, it is **not known in which direction the reforms will go, apart that they are will incorporate ideas of green transition and digitisation**. Statements from coalition partners show big differences in their views. When talking about the tax reform coalition partner the Left party wants to rise contributions paid by employers and believes that the tax burden should be transferred from working people to capital and property. The Left leads the Labour ministry, and their minister Luka Mesec has been vocal about such ideas.

- Finance Minister Klemen Boštjančič, on the other hand, points out OECD recommendation to reduce the tax burden on labour. In his opinion there is room for increasing the taxation of consumption and property, as well as "many other things". Prime Minister Golob has named a few strategic councils and consultative working groups that are to prepare the proposals.

Public sector wage system under threat of strikes

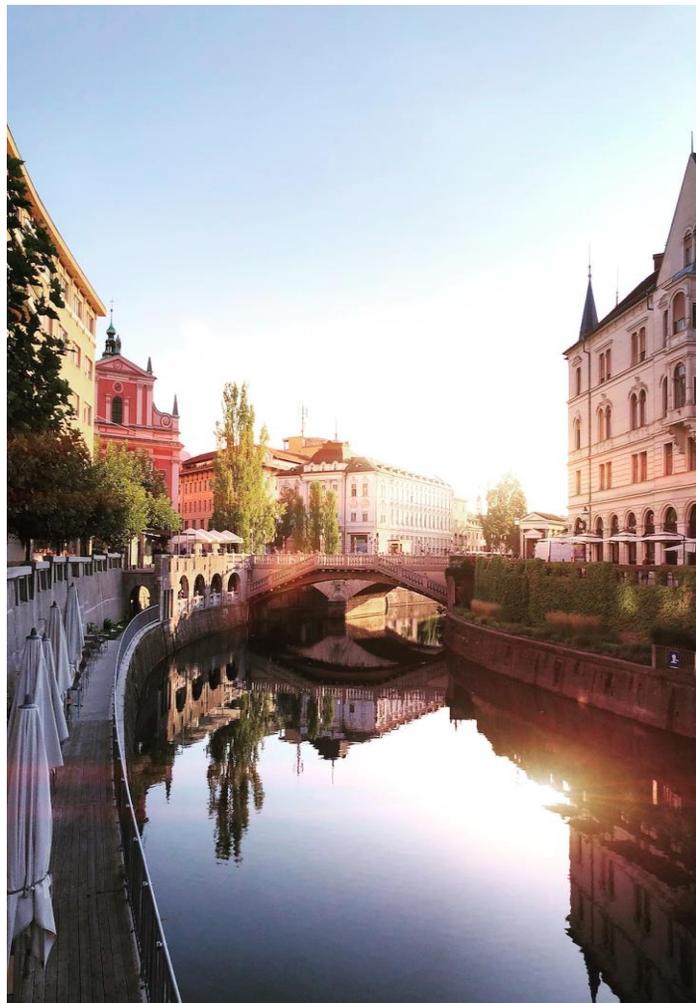
- Partial agreements for salary increase agreed between the government and representatives of healthcare workers and promises of a high monthly allowance for officials in the judiciary have opened the Pandora's box of the **public sector uniform wage system**. Representatives of other work groups, like firefighters, police and others, but also pensioners, have already stated their **expectations for rises in wages and threatened to go on a strike**. The Government has subsequently announced a reform of the uniform salary system in the public sector.
- Governor of Bank of Slovenia Boštjan Vasle has warned of risks on the side of wage pressures, while the Fiscal Council assessed that the planned government budget deficit in Slovenia is already among the highest in the EU even without the announced extra wage rises in the public sector.

With a strong coalition better possibility for constitutional changes

- Slovenian President, Nataša Pirc Musar, started discussions with the presidents of the parliamentary parties and the heads of parliamentary groups on strategic topics on which a consensus is

needed for the future of Slovenia. Among other things, they demand constitutional changes. For the first time in many years the current coalition could gather enough votes to pass constitutional changes.

- At the first meeting with the new President a **discussion was held also regarding changes to the electoral system, the appointment of judges, ministers and other high officials**. President Pirc Musar will meet separately also with representatives of the opposition to test if there is the possibility to gain also support from the opposition to key planned changes of the constitution.
- President Pirc Musar and Prime Minister Golob announced they will be meeting regularly to discuss topics important for the future of the country.



Memorable quotes

Last year was undoubtedly full of crucial political events, which have left a deep trace in the European political scene and have changed the course of history. It was also a year of memorable quotes from CEE politicians, from the historic to the comedic. Here's a sample of our favourites:

Poland

President Andrzej Duda was the first leader of a foreign country to speak in the Ukrainian parliament since the beginning of the Russian aggression on Ukraine (22 May 2022):

"I am today in a beautiful proud city of Kyiv, the capital of free, independent, democratic Ukraine, which for almost 90 days has been putting up heroic resistance to barbaric aggression. I was here also on 23 February, just a few hours before Russian invasion began. I was there to support Ukraine and its people at an extremely difficult time, and to assure you that Poland would never leave Ukraine alone. (...)

I would like to let you know that your loved ones: spouses, parents, children, grandchildren, those millions of people who had to leave Ukraine, fleeing the tragedy of war, also to Poland – are not refugees in our country. They are our guests. (...)

I stand to express our thanks to you. So far you have been thanking us. You say that Poland has opened its borders for 3.5 million Ukrainian refugees and became home to more than 2 million. It is true. You say that Poland has supplied Ukraine with huge numbers of tanks (...) However, we are not the heroes. It is you who are the heroes. (...)"

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Hungary

Prime Minister Viktor Orbán said at the night of the election:

"We have won a great victory – a victory so great that you can see it from the moon, certainly from Brussels."

Slovakia

Richard Raši (Member of the parliament from the Hlas-SD) to Denník N's survey question "What should be done to reduce alcohol consumption in Slovakia?"

"The first measure for Slovaks to drink less must be early elections."

Serbia

During the pre-election TV Show, in March 2022, Serbian **President Aleksandar Vucic** came out of the refrigerator on the stage and on that occasion stated: "I bore everyone so much that people think I'm coming out of the fridge."

Bulgaria

Speaker of the House addresses a colleague MP, during the first session of the Parliament:

"Mr Chenchev, it will be way funnier from now on!"



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