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Allianz Research

What to expect from the European elections

Executive Summary

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- **With an expected 60% participation rate, the 2024 EU elections are set to be a pivotal moment for the European Parliament.** Addressing poverty (33%) and public health (32%) are voters' top priorities, according to the April 2024 Eurobarometer survey, while the top five topics that emerge from political parties' manifestos are climate and energy, security and defense, competitiveness and growth, foreign policy and fiscal and industrial policies. We expect the main centrist parties to still secure a majority of the 720 seats, but right-wing parties are likely to secure more support, which could alter the EU's legislative priorities and overall direction on some topics, notably security and defense.

- **The next EU Commission should prioritize enhancing EU competitiveness, revamping foreign policy on trade, fortifying defense and security, addressing climate change and strategizing fiscal policies.** To boost competitiveness, the EU needs to foster a culture of innovation, increase investment in R&D and embrace digitization and AI to drive productivity gains. On foreign policy, the EU needs to focus on its strength in trade and strive for a dual strategy of new FTAs and smaller bilateral agreements on specific topics that are easier to reach but often important in impact. On defense and security, policies must adapt to a changing security landscape and reallocate resources from within the EU budget to common defense spending. Meanwhile, fiscal policy needs to become more strategic with a long-term vision that supports strategic industries, economic stability and growth through counter-cyclical spending and taxation policies as well as structural reforms for upcoming investment needs related to the climate transition (more than 3% of GDP) and defense and security (above 2% of GDP).

- **The EU also needs to strive for a truly integrated Single Market in energy, telecommunications and the financial sector.** A Capital Markets Union has never been more urgent as competition for capital intensifies amid higher interest rates and immense investment requirements. While single supervision remains out of the scope, measures to reduce the regulatory burden, improve financing conditions for EU businesses by reviving the securitization market, harmonize insolvency law, accounting practices, listing requirements and strengthen supervision are crucial**.**

- **On climate policy, after the great leaps of the European Green Deal and Fit for 55, the next five years should be all about implementation. However, the energy market still needs a clear plan.** Over the last five years, the EU has embarked on a transformative journey with the implementation of a comprehensive European Green Deal and Fit for 55, aimed at reducing net greenhouse gas emissions by at least -55% by 2030 compared to 1990 levels (currently at -32%), positioning itself as a leader in the global fight against climate change. This sets the stage for the years to come and current items on the agenda need implementation, so we do not expect any further big reforms on the climate front. However, the energy market still needs a clear plan, i.e. a truly European grid plan. After long negotiations, the EU Council enacted the long-awaited electricity and gas market reforms in May 2024. Unfortunately, it falls short on several key aspects and does not deliver harmonized and long-term focused EU electricity market framework.

A new political cycle

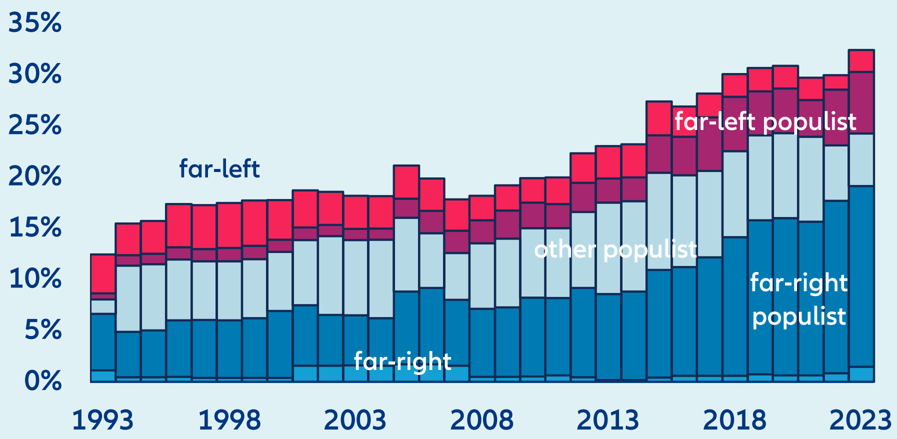
The 2024 European elections could draw a higher voter turnout than usual, albeit still below national elections, with 60% of voters going to the polls. From 6 to 9 June, more than 400mn European citizens across the 27 EU member states will elect 720 members of the European Parliament for the new mandate 2024-2029. The turnout for EU elections is usually low (around 50% in 2019) but the spring 2024 Eurobarometer survey indicates that this year's elections could draw a voter turnout of 60%, though this is still low compared to national elections. Voters tend to perceive the European elections as an opportunity to address national politics but they play a significant role in shaping laws, with wide-ranging implications for citizens and businesses alike.

We expect the outcome to follow a similar pattern to recent national votes, with a surge in right-wing parties. While the biggest political groups, EPP and S&D, are on track for a stable outcome compared to 2019, the right spectrum (ECR and ID) will increase while the Greens and Renew will suffer significant losses. As the center-left is expected to significantly decrease compared to the 2019 outcome, the EPP is again needed to find a workable majority in the European Parliament. This more right-centered European Parliament will be more polarized and uncertainties over which alliances politicians favor could increase.

Box 1: The rise of populist parties in Europe

European populist parties have more than doubled their vote share in the last 30 years. The share of populist parties in European national elections increased to 32% in 2023, from 23% a decade ago and 18% two decades ago (Figure 1). Out of the 10 last elections in EU member states, nine were won by right-leaning parties: Portugal, the Netherlands, Slovakia, Spain, Greece, Finland, Bulgaria and Italy. The only exception since 2022 has been Poland. This has significantly shifted the European political landscape and its policy priorities.

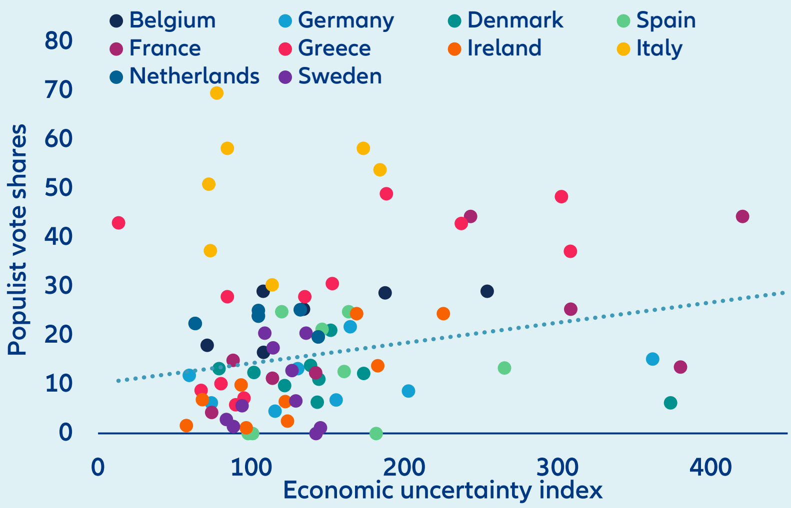
Figure 1: Share of populist parties in national elections in European countries, in %



Sources: Party classification from the PopuList 3.0, vote shares from Parlgov and the World Bank, Allianz Research

Uncertainty is a main contributor to the increase in populist vote shares, even though many other underlying factors play a crucial role as well. We find that higher economic policy uncertainty has triggered higher populist vote share outcomes in European national elections, and the other way around (Figure 2). About 15.6% of the surge in populist vote shares can be explained by higher economic policy uncertainty. This is created not only by geopolitical tensions, uncertainty on foreign relations or war scenarios, but also by policy changes undertaken at the national level, such as insecurity about energy supply, a surge in inflation and consequent loss in consumers' purchasing power. However, the green transformation and implications on people's personal lifestyles also contribute. In this context, politics plays a crucial role: any back and forth or unclear communication on the path of the energy transition or short-notice withdrawal of support measures can add to economic uncertainty. This opens the door to populist parties that often offer simple but illusionary solutions to rather complex problems (such as climate change or immigration).

Figure 2: Share of populist parties in national elections in Europe, in %



Sources: Party classification from the PopuList 3.0, vote shares from Parlgov and the World Bank, Allianz Research

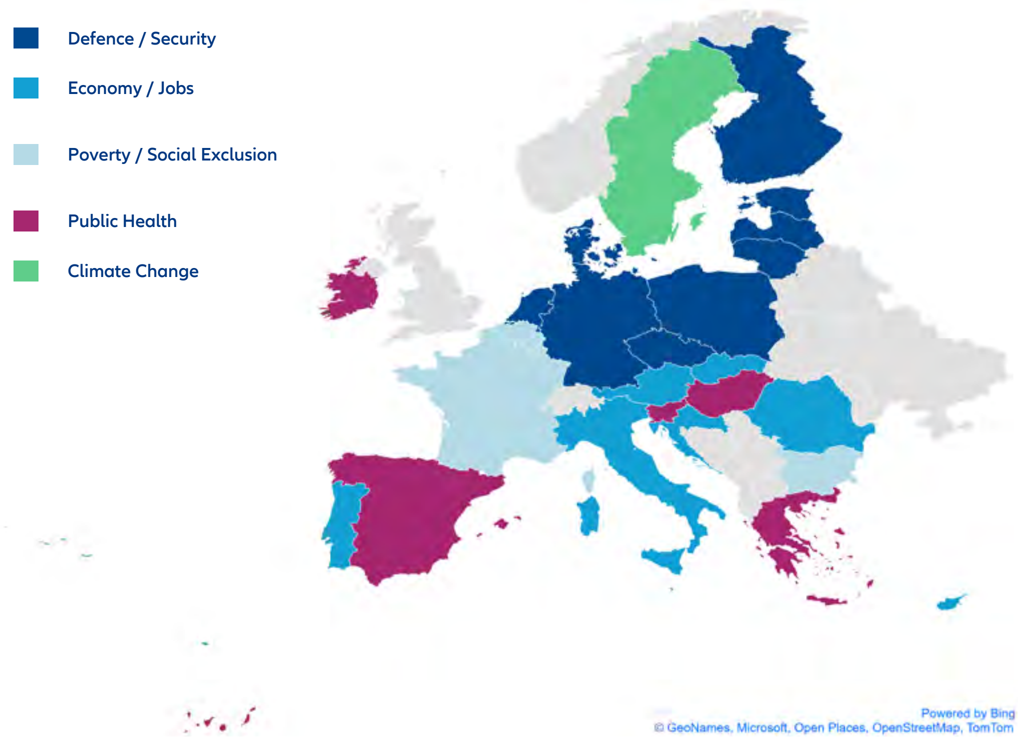
What Europeans want

Addressing poverty and improving healthcare are the top priorities for voters. According to the Eurobarometer survey of April 2024, poverty was identified as a primary campaign concern by 33% of respondents, closely followed by public health at 32%. The economy, job creation, defense and security were all equally important issues, each selected by 31% of participants. Interestingly, addressing climate change, which had previously ranked third in importance in the late 2023 survey, fell to fifth place with 27% of respondents highlighting it as a key issue. These results are in line with our own survey, the Allianz Pulse: The economy, jobs and inequality are top of mind, while the green transformation plays only a minor role.[1] Austria is the only country where the future of Europe won out. Climate change was named a top priority in Sweden, while Eastern and Northern Europe, including Germany, are dominated by the debate on defense and security (Figure 3).

Parties do focus on some priority topics – but not all of them match. Looking at the election manifestos of pan-European political parties, we find that there is some overlap with voters' concerns. The top five topics that emerge are climate and energy, security and defense, competitiveness and growth, foreign policy and fiscal and industrial policies (Figure 4).

Overall, EU politics could be affected by the presence of more Eurosceptics in the European Parliament. The major centre parties (EPP, S&D and Renew) all share similar focus topics on economic aspects. But as a result of increased pressure from the far right, their attention has also slightly shifted towards more right-wing priorities, including security and defense. Economic priorities indicate a focus on competitiveness and growth followed by foreign policies as well as fiscal and industrial policies. On the social aspects, health and the creation of jobs dominate, followed by immigration. With more "hard" than "soft" Eurosceptic forces potentially influencing European debates, this could alter the EU's legislative priorities and overall direction on some of the topics. But majorities and coalitions on EU level are more heterogeneous and complex than in national politics. When it comes to coalitions, it is usual to see political groups coalesce with different parties depending on the topic at hand.

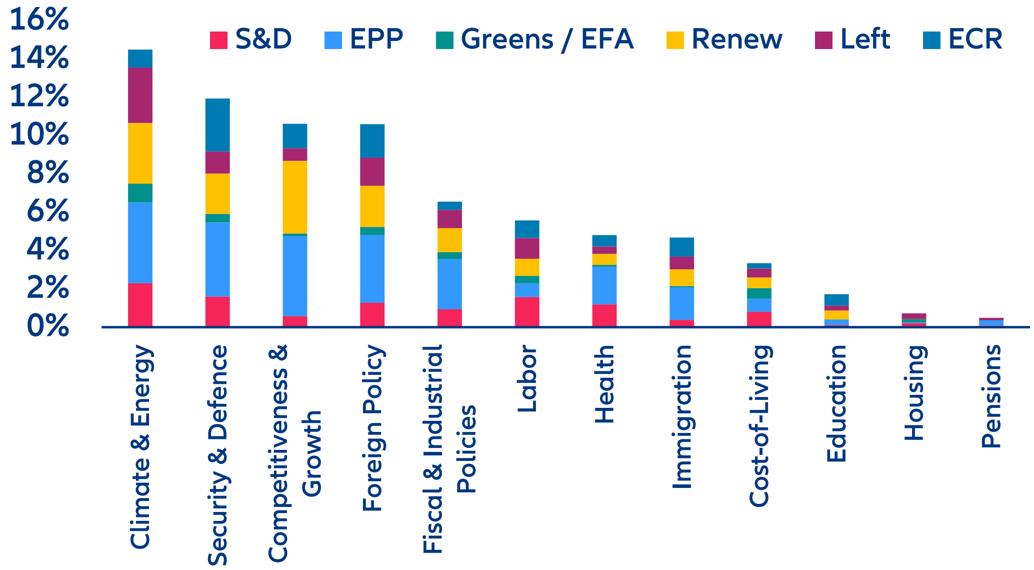
Figure 3: Key topics as prioritized by the EU population based on survey data



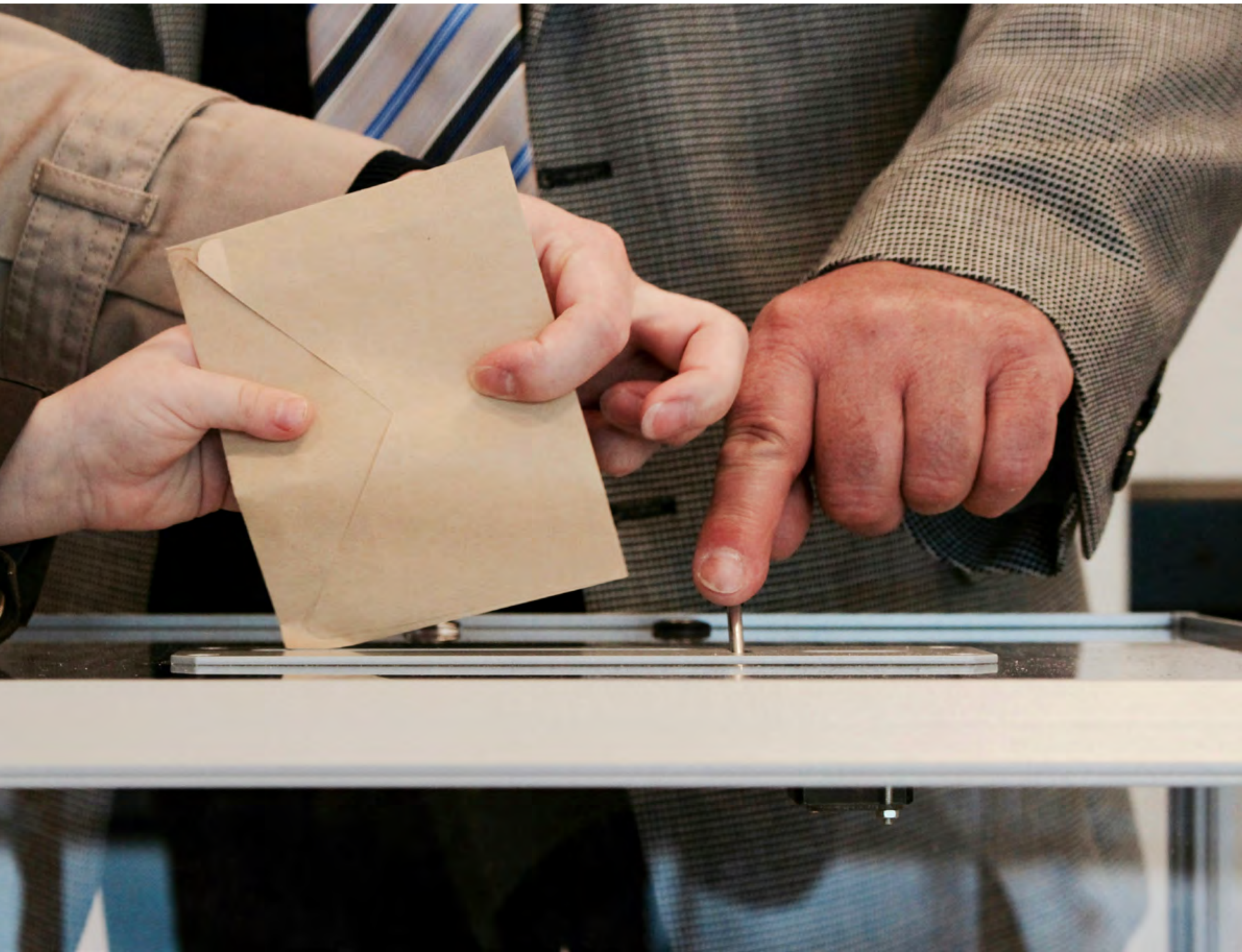
Sources: Eurobarometer 101.1, Allianz Research

[1] See Allianz Pulse 2024: What unites and separates the demos of Europe.

Figure 4: Analysis of the political manifestos, % of total

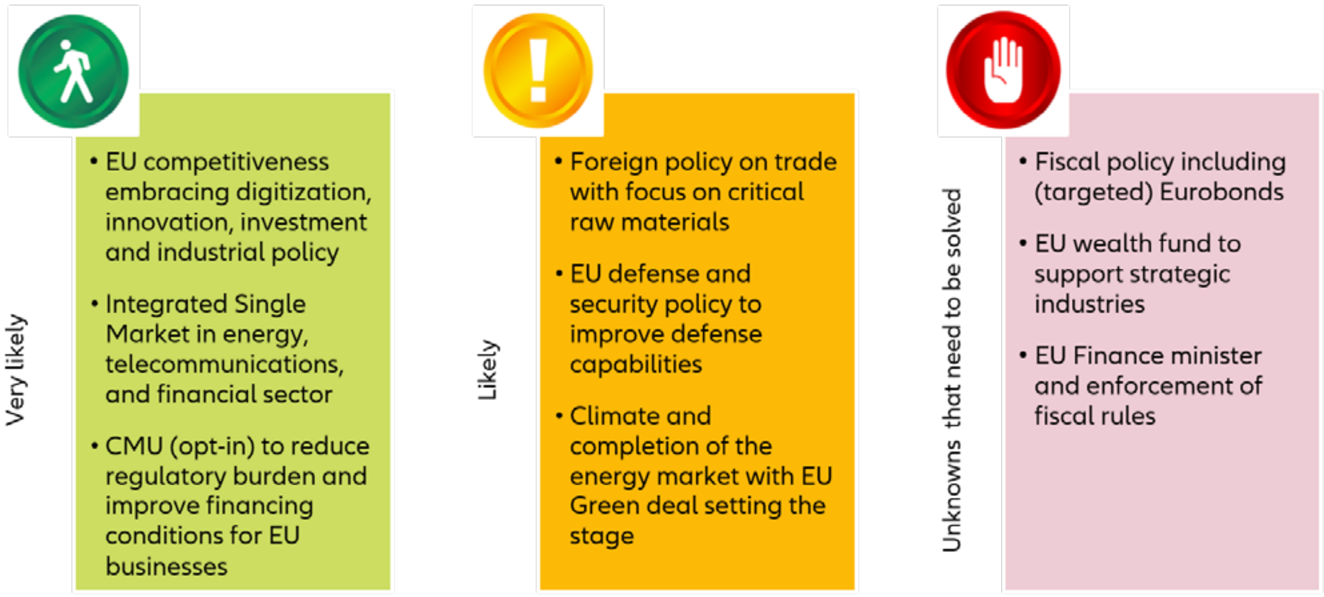


Sources: Party manifestos, Allianz Research. Note: Share of word count in relation to total words analyzed within all manifestos. Topics are not context driven in this word analysis and may be used in positive or negative context.



Looking back, looking forward: Where does the EU Commission go from here?

Figure 5: Key topics that should be on the EU Commission agenda grouped by likelihood of getting a consensus in the next five years



Source: Allianz Research.

Over the last five years, the European Parliament has established a digital agenda focused on creating a competitive digital economy through investments in infrastructure, skills development and innovation in Artificial Intelligence (AI) and cybersecurity. The goal has been to provide secure digital services while protecting privacy rights and upholding fundamental values. As a result, in 2022, the EU agreed upon the Digital Markets Act to ensure fair competition among online platforms, leading to benefits like lower prices and innovation. In line with this, the Digital Services Act promotes trust, innovation and growth in digital services through EU-level supervision, complementing national regulators to create a safe online environment for all citizens. The EU also passed the world's first AI law in March 2024, establishing a regulatory framework that promotes safe and EU-aligned systems through a risk-based approach.

But to foster a culture of innovation and reduce risk aversion, it is crucial to simplify regulations, enhance competitiveness and promote growth. A major point for the EU is to embrace digitization and AI to drive productivity gains, while increasing investment in R&D and education to boost future productivity levels. For decades, European industry has predominantly focused on specialization mid-tech sectors with a moderate level of R&D intensity. This path dependency has made it challenging for the EU to keep pace with high-tech industries, including AI and biotech revolutions. Addressing this challenge requires public-sector intervention to stimulate research in new technologies and foster the growth of EU high-tech industries. Five budget-neutral shifts are necessary to fund innovation in Europe going forward: (i) enhancing European Investment Council (EIC) governance by recruiting independent, skilled program managers with increased decision-making authority, and simplifying processes and the design procedure to enable scientists to vote on best proposals; (ii) gradually downsizing the European Institute of Innovation & Technology (EIT) and European Innovation Ecosystem (EIE), which would free up to EUR0.51bn annually from soon to be self-sustaining current projects; (iii) freeing up EUR0.41bn per annum for innovation projects from the Accelerator budget, currently used for investment rather than innovation; (iv) allocating the resulting EUR1bn per year to US Advanced Research Projects Agency (ARPA)-style projects; and (v) utilizing resources from Pillar II clusters and Innovation Fund to fund Pathfinder-type programs or establish two thematic agencies for energy and health[2].

At the same time, industrial competitiveness and a focus on integration as the foundation of growth and prosperity in Europe are also important. There have been several initiatives to support investment in the EU since 2019 (eg. the Recovery and Resilience Facility, Next Generation EU fund and the RePowerEU plan, Table 1) but they have had little positive impact for now, given slow implementation. Even though industrial policy is high on the agenda of many countries, governments must avoid picking winners and engaging in protectionism or subsidies that hinder market efficiency and trade within the EU. To boost competitiveness, the EU should strive for a truly integrated Single Market, particularly also in energy, telecommunications and the financial sector. Especially for financial services, a Capital Markets Union (CMU) has never been more urgent as competition for capital intensifies amid higher interest rates and immense investment requirements. While single supervision remains out of the scope, the ongoing debate could include measures to reduce the regulatory burden and improve financing conditions for EU businesses by reviving the securitization market, increasing harmonization (insolvency law, accounting, listing requirements) and strengthening supervision.

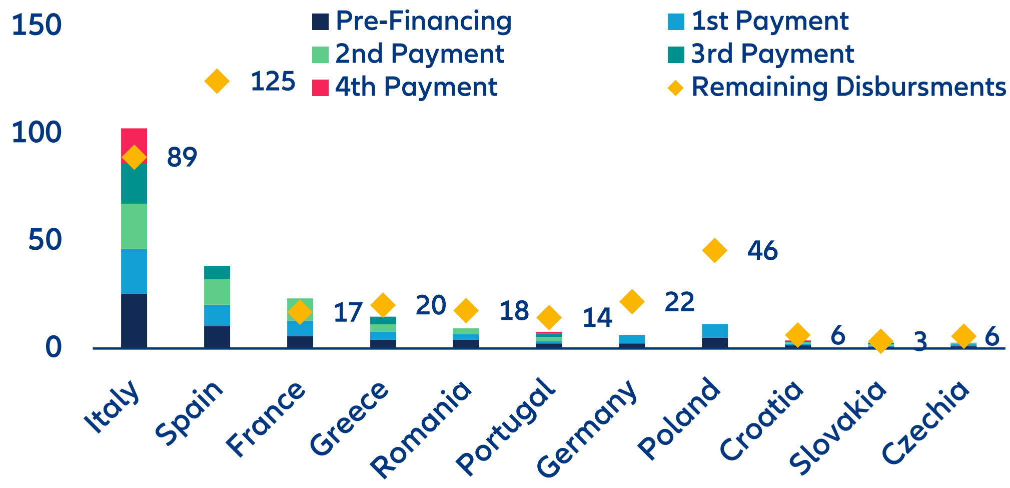
Table 1: Measures the EU has taken to strengthen investment since 2019

Programme	Description	Budget/Goal
InvestEU Programme	Consolidates various EU financial instruments to stimulate investment in innovation, research, and infrastructure.	Aim to trigger EUR650bn in investment
European Fund for Strategic Investments (EFSI)	Part of the Investment Plan for Europe, aimed at mobilizing private investment for strategic projects.	Targeted to mobilize EUR500bn by end of 2020
Connecting Europe Facility (CEF)	Funds infrastructure projects in transport, energy, and digital services sectors.	EUR33.7bn for 2021-2027
Capital Markets Union (CMU)	Aims to integrate capital markets across the EU to diversify funding for businesses and improve access to capital.	N/A
European Structural and Investment Funds (ESIF)	Reduces regional disparities and supports economic cohesion through funding for various projects.	EUR373bn for 2021-2027
NextGenerationEU	A recovery instrument to support the EU's recovery from the COVID-19 pandemic.	EUR750bn
European Green Deal Investment Plan	Mobilizes sustainable investments to achieve climate neutrality by 2050.	EUR1trn over a decade
RePowerEU	Aims at diversifying gas supplies, speeding up the rollout of renewable energy, improving energy efficiency, electrification and deployment of heat pumps, investing in future-proof technologies and strengthening emergency measures	around EUR300bn of investments by 2030

Sources: European Commission, Allianz Research.

[2] Further details can be found in Clemens Fuest, Daniel Gros, Philipp-Leo Mengel, Giorgio Presidente, and Jean Tirole: "EU Innovation Policy – How to Escape the Middle Technology Trap?" EconPol Policy Report, April 2024.

Figure 6: Next Generation EU by tranche, EURbn



Sources: European Commission, Allianz Research.

Between 2019-2024, EU trade policy achieved significant milestones in promoting a more open and sustainable global trading system. The EU has signed several free-trade agreements (FTAs) with key partners such as Japan (2019), Singapore (2019), Vietnam (2020), UK (2021), and New Zealand (2024) that have opened up new market opportunities for European businesses while upholding high standards in areas such as labor rights and environmental protection. Currently the EU has 46 FTAs in force that covered 44% of its extra-EU trade in 2023 (48% of exports and 40% of imports). Including the EU27 itself, free trade covers more than three-quarters of the bloc's total trade.

Europe has also positioned itself through a common strategy on critical raw materials. In November 2023, the EU Critical Raw Materials (CRM) act to strengthen the CRM supply chain, diversify imports, monitor and mitigate risks and promote circularity and sustainability was adopted. It includes creating a list of strategic raw materials, establishing strategic projects in third countries and promoting sustainable practices in raw material projects. The focus is on metals and reusability of CRMs to move towards a circular economy. Member states are encouraged to cooperate and develop national authorities for project implementation, with support from the Commission. Companies are urged to audit their supply chains and report to mitigate supply risks. Overall, the proposal aligns with the European Green Deal strategy and aims to ensure environmental protection and reduce dependencies on imports. Among the G7 and Australia, the EU leads in the signing of bilateral agreements connected to supply chains related to critical materials crucial for the green transition (Figure 7).

Box 2: Unpacking Letta's report on the future of the EU's single market

On 18 April, former Italian prime minister Enrico Letta published his long-awaited report on the future of the EU's single market, entitled "Much more than a market. Speed, Security, Solidarity. Empowering the Single Market to deliver a sustainable future and prosperity for all EU Citizens". The report was based on over 400 stakeholder meetings and urges policy action for the new European political and institutional cycle 2024-2029 in several areas such as the financial, energy and telecommunications sectors – identified as key – as well as defense, economic security and enlargement policies.

It discusses the evolution of the European Single Market and its need for modernization in the face of the current global challenges. The Single Market was established when the EU and the world were less complex and integrated, and today it must adapt to a world that has grown "larger", with significant economic, demographic, and geopolitical shifts. Letta's report suggests the addition of a "fifth freedom" to the existing four (movement of people, goods, services and capital) on research, data, knowledge, competences, innovation and education.

A central theme of the report is the "fair, green, and digital transition," which is crucial for the EU's future. It calls for mobilizing private capital, refining the approach to state aid and leveraging European public investments to support this transition. Looking more into the details, the Letta report discusses the concept of a Savings and Investments Union to address the inefficiency in the use of the EU's capital surplus through key measure such as: (i) transforming the Capital Markets Union into a Savings and Investments Union to better leverage European private savings and attract additional resources from abroad; (ii) mobilizing private capital within the EU to finance a fair green and digital transition; (iii) creating a state aid contribution mechanism for pan-European initiatives to prevent further fragmentation within the EU.

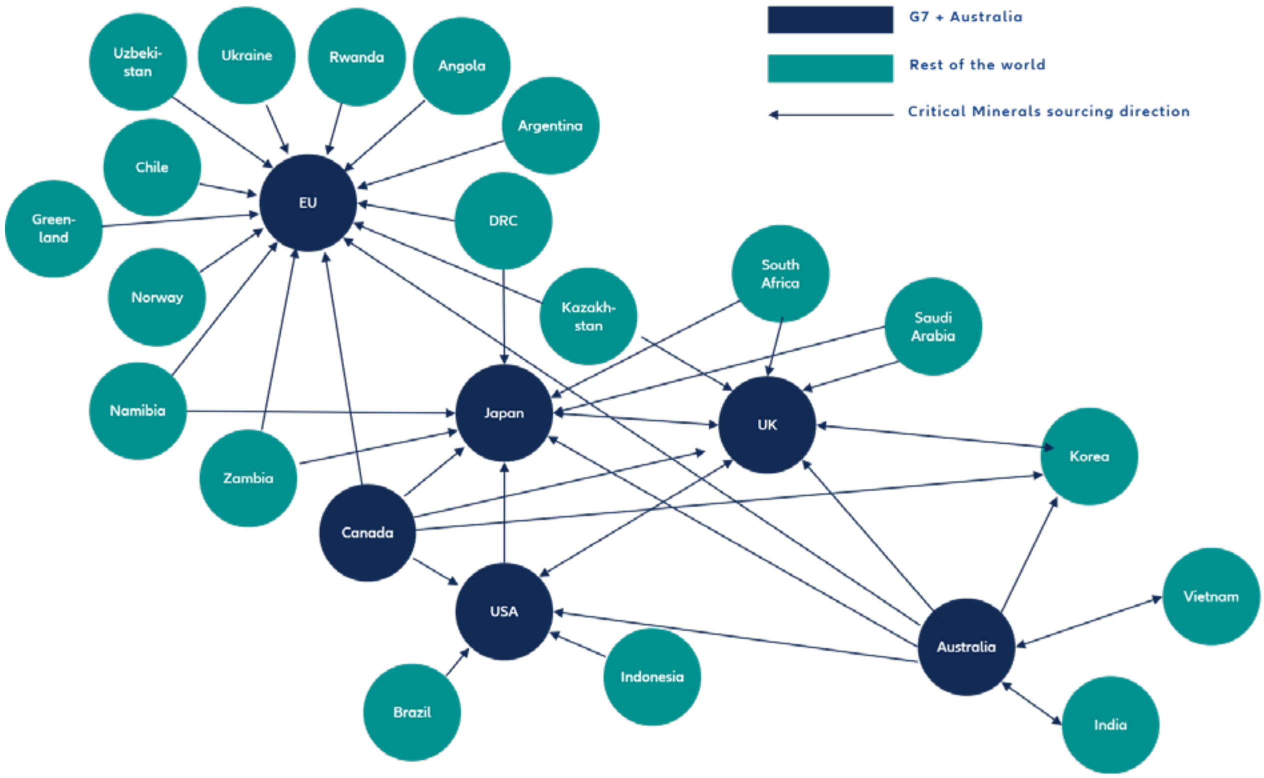
The report also discusses the need for a Single Market that supports job creation and makes doing business easier, addressing bureaucratic burdens and regulatory fragmentation that affect European businesses. It proposes a European Code of Business Law that would function as a 28th regime to give firms an alternative to complying with existing national codes and allow for quicker Europeanisation. Letta is calling for greater use of Regulations rather than Directives, to ensure harmonized EU law, along with measures to crack down on gold-plating of Directives during national implementation. Second, it calls for greater harmonization of different forms of EU-level bond issuance to create a single asset class (i.e., bonds issued by Commission, EIB, ESM). The report also proposed a new regulatory architecture for digital markets, drawing inspiration from the Eurosystem of central banks and the EU's AI office – sending the signal that a new supervisory system is to be created in this space. In addition, a dedicated EU fund for financing cross-border digital infrastructure is proposed.

The report also addresses the issues of enlargement and security. It emphasizes that enlargements have historically benefited the EU and that a careful approach to future expansions is necessary to ensure stability. On security, the report stresses the need for a unified EU defense market and innovative financing options such as defense Eurobonds to modernize EU defense capabilities.

Finally, the report underlines the importance of the Single Market's social dimension, ensuring that all European citizens benefit from shared prosperity and that policies promote social justice and cohesion. It advocates for the freedom to stay, where high-quality jobs are available locally, and for greater SME participation in the Single Market.

In conclusion, the report calls for a bold strategy for the future of the Single Market to ensure it remains a driver of sustainable development and prosperity, giving Europe the leverage to compete effectively in a rapidly changing world.

Figure 7: G7 + Australia bilateral sourcing agreements connected to critical materials signed since January 2020

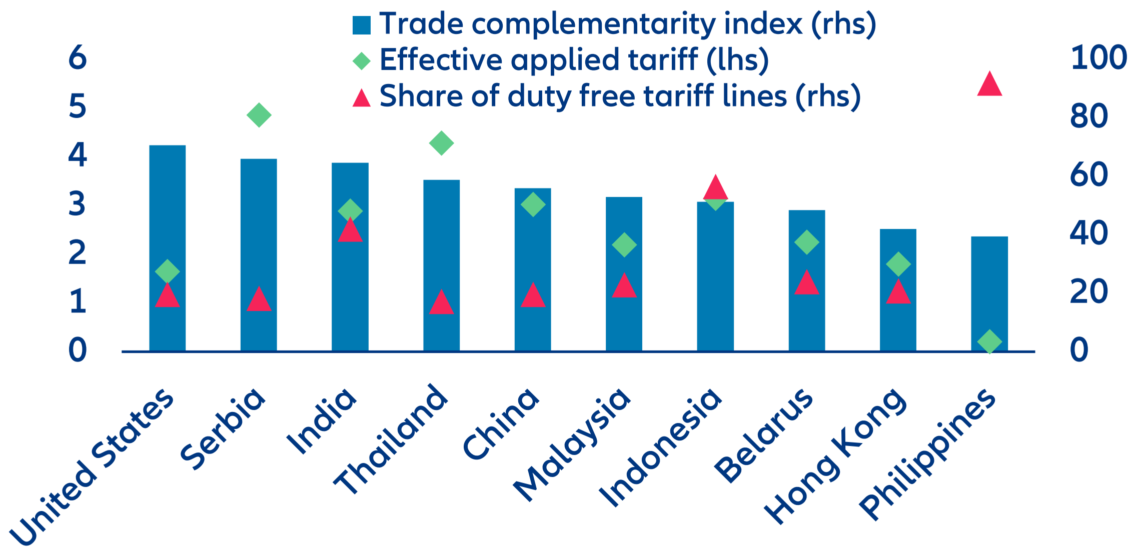


Sources: EU Commission, Australian, Canadian, Japanese, Korean, UK and US governments, Allianz Research.

However, global shifts like geopolitical changes and protectionism will necessitate a further review of the trade strategy. Upcoming foreign policy on trade needs to square the circle between traditional FTAs and smaller topical agreements that are easier to reach. Already negotiated trade agreements need to be concluded and ratified (such as with Mercosur, Australia or India). But French farmers, for example, very much object a deal with the Mercosur countries or Australia due to their strong focus on agriculture and beef production. To push things through, the EU needs to low ball on some of the topics. Nevertheless, the EU must pursue new FTAs (i.e. with African countries), especially to secure critical raw materials needed for the green transition or green energy. Looking at the trade complementarity index[3] (TCI), the top ten trade partners for the EU to pursue an FTAs with would be the US, Serbia, India, Thailand, China, Malaysia, Indonesia, Belarus, Hong Kong and the Philippines (Figure 8). But while effectively applied tariff rates are still high with Serbia (4.9%), India (2.9%), Thailand (4.3%) or Indonesia (3.1%), those for the US or the Philippines are on average already very low. The share of duty-free tariff lines is higher for India (effective 42% compared to 18% MFN duty free tariff lines) or Indonesia (56% effective versus 18% MFN). Overall, not all these economically favourable agreements are politically feasible, but diversification of supply chains should nevertheless be propagated through EU trade policy as sovereignty stands against mounting geopolitical tensions and protectionist tendencies. Another strategy that should be pursued in addition are specific bilateral agreements on topics such as critical raw materials or green energy. This is in general an interesting complement to the EU trade policy as 61% of EU exports and imports are traded duty-free already while EU trade faces an average effective tariff rate of only 1.5% (2.9% MFN tariff rate mini deals that tackle technical barriers to trade which often constitute significant trade costs. Such agreements are easier to reach than a full FTA. Two examples for mini trade deals that should be high on the agenda of the new EU Commission are Mutual Recognition Agreements (MRAs) between the EU and the US. MRAs already exist covering telecommunications, pharmaceuticals, medical devices, electromagnetic compatibility, or electrical safety. But an EU-US machinery MRA subject to trade cost reduction of EUR190bn and an EU-US Clean Tech MRA worth EUR220bn would significantly reduce certification costs – typically higher than existing tariffs in the EU and US on these products. Due to the trade flows at stake, these mini trade agreements could become big deals.

[3] The TCI measures to what extent the export profile of one country matches the import profile of another country. The higher the index the better the trade profiles match. We resonate that countries with a higher match should pursue FTAs to benefit from complementarities.

Figure 8: Potential top ten trade agenda according to trade complementarity index, effectively applied tariffs and share of duty-free tariff lines, in %



Source: WITS, World Bank, WTO RTA gateway, Allianz Research.

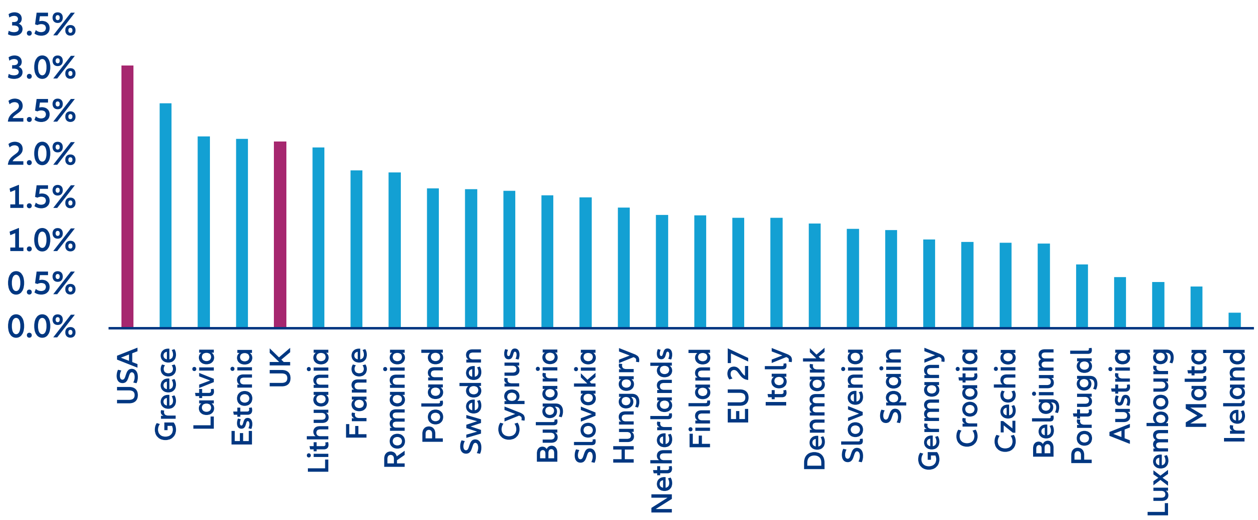
Challenges in the European security architecture, including conflicts near NATO's Eastern border and growing instability in the region, underscore the need for adaptation. Since 2019, the EU's approach to security and defense has hinged on three pillars. First, the EU Security Union Strategy, launched in July 2020, which focuses on enhancing security in physical and digital domains through open strategic autonomy for critical products and technologies. Second, the Strategic Compass for Security and Defence, introduced in 2022, which aims to bolster the EU's response to various security threats like cyber-attacks and terrorism by prioritizing military mobility, cybersecurity enhancements, increased defense spending among member states and early crisis management capabilities. The third pillar focuses on economic security to enhance the EU's technological sovereignty, research security and economic resilience by promoting cooperation with third countries. These three pillars are complemented by the 2024 European Defense Industrial Policy, which focuses on ramping up production capabilities, fostering innovation and promoting collaboration among member states in defense spending.

It is clear that the EU needs to increase defense spending fast and create fiscal space for a permanent rise beyond 2% of GDP. Some governments have already announced aims for this (e.g. Germany, France, the UK). But as many countries accumulated a lot of debt and thus do not have enough fiscal leeway, European governments face trade-offs as they also need to invest in transforming their economies and making them more competitive. Europe, hence, finds itself in a dilemma which can be solved only if four principles are followed. (i) Implementing growth-friendly policies to free resources, easing the trade-off between defense spending and other spending categories. (ii) Keeping sustainable public finances to help raise defense spending. (iii) Being more restrictive on consumption spending by identifying policies that are inefficient and do not fulfil important government functions, thus freeing fiscal space for defense spending. (iv) Strengthening defense as a European public good. Reallocating resources from within the EU budget to common defense spending would send a strong signal, as well as pushing for targeted Eurobonds. Such reallocation would underline Europe's willingness to adjust to a new security environment.

There was no real fiscal and financial integration between 2019-2024, but some progress has been made on the fiscal rules, necessitated by Covid-19 and geopolitical tensions. The new set of rules adopted in 2024 requires member states to prepare fiscal plans that span over four to five years, aligned with a reference trajectory for net expenditure developments along specific government debt (60% of GDP) and deficit (3% of GDP) thresholds. This approach aims to ensure sustainable fiscal trajectories and prudent debt levels over a four-year adjustment period.

Looking ahead, fiscal policy will need to become strategic. Fiscal policies are among top five most mentioned topics in campaign manifestos as all parties are conscious about the need to reassure inventors about the credibility of their fiscal plans. To date, the fiscal policy adjustments will shave -1pp from European GDP growth in 2024-25 cumulatively. However, additional efforts are needed as debt sustainability will still be an issue (r-g is likely to surprise on the upside). We think that fiscal policy will need to obey three key principles, though the ambitions of the future legislature will probably fall short of these needs. 1/ Central fiscal capacity at the EU level, such as a European Wealth Fund to support strategic industries, or targeted Eurobonds for specific projects in defense and/or to support the climate transition. 2/ Strategically flexibility, i.e. fiscal policy should support economic stability and growth. This involves counter-cyclical spending and taxation policies to smooth out economic fluctuations, as well as structural reforms to improve the potential growth rate of the economy. The Stability and Growth Pact (SGP) also needs to keep a certain flexibility. 3/ A long-term strategic vision, in order to support the upcoming investment needs related to the climate transition (more than 3% of GDP) and the increase in spending for defense and security (above 2% of GDP). However, we do not foresee any tangible progress on common EU debt in the next five years. Enforcement of fiscal rules remains a challenge, and prospects for a Fiscal Union with an EU finance minister are not in sight.

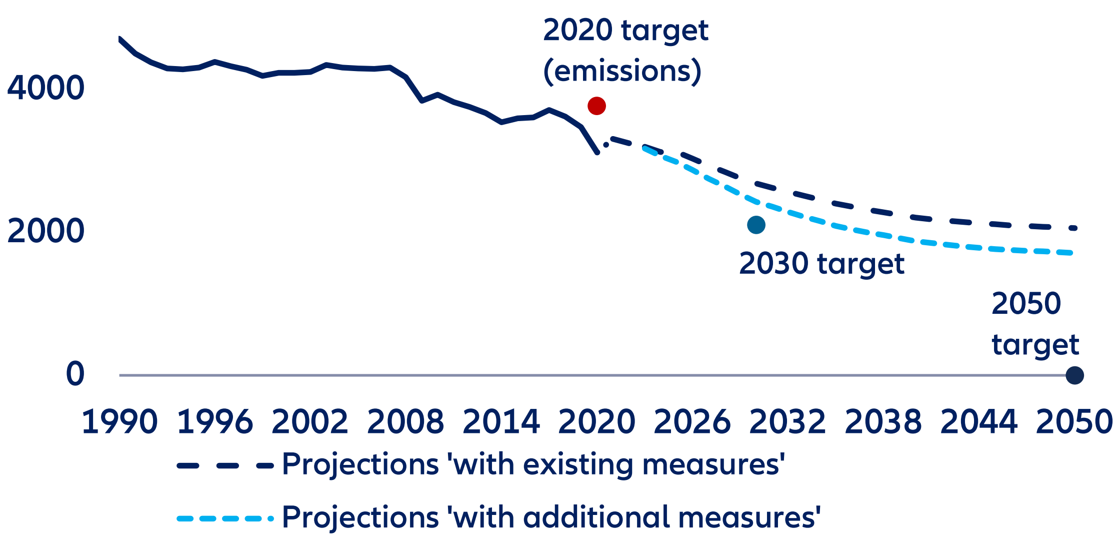
Figure 9: Government expenditure on defense (COFOG) in 2022, in % of GDP



Sources: OECD, Allianz Research.

The EU has positioned itself as a leader in the global fight against climate change, but we do not expect a further acceleration in climate policies. Besides the implementation of a comprehensive European Green Deal, the goal of achieving net-zero greenhouse gas emissions by 2050 has been enshrined in the legally binding European Climate Law, and under its Fit for 55 strategy, the EU created the world's first and largest carbon market, designed to reduce greenhouse gas emissions cost-effectively. The EU has also set binding renewable energy targets to ensure that renewable energy makes up at least 32% of the EU's energy mix by 2030, adopted the Clean Energy for All Europeans package to promote energy efficiency and adopted a Circular Economy Action Plan to promote circularity in product design, production and consumption. But while all parties in the grand coalition have made climate topics a priority, the political will and public support for a more ambitious climate agenda is fading. The EU Green Deal sets the stage for the years to come and the current items on the agenda need implementation.

Figure 10: Progress towards achieving climate targets in the EU27, mn tons of Co2 equivalent (MtC2e)*



Sources: EEA, Allianz Research; Note: The 2022 value is based on approximated inventory reports.

We also do not expect the completion of the energy market. The EU Council adopted the long-awaited electricity and gas market reforms in May 2024 after they were enacted by the EU Parliament end of 2023. It allows member states to use Power Purchase Agreements (PPAs) and Contract for Difference (CfDs) to stabilize domestic prices, and also offers the Council the power to declare an electricity crisis, which in turn would allow member states to take support measures. It is a first step towards a deeper transformation of the EU's electricity market but it falls short in several key aspects. The energy market needs a clear plan, i.e. a truly European grid plan. More competitiveness, private market involvement and more targeted actions could help to push necessary energy market investments through. The Commission estimates that around EUR584bn in investments are necessary for electricity grids in this decade alone[4]. Emphasis should be placed on accelerating network deployment and modernization by encouraging construction, revising administrative procedures and facilitating financing. Efficient management of network assets and adequate planning are necessary, integrating networks on land and at sea and increasing interconnectors between EU and non-EU countries. In the next six years, cross-border transmission infrastructure should double, which would result in decreasing generation costs by EUR9bn annually until 2040. For electricity there is also a need to simplify the introduction of capacity markets to allow for necessary investments and rapid development of flexibility markets. Strengthening locational signals would allow efficient allocation of generation and storage sources, better grid use, and optimal location of new large consumers. Locational pricing could save EU consumers money spent on unnecessary infrastructure. However, these measures are unlikely to be fully targeted by any of the majority scenarios as national interests will continue to prevail.

Finally, it remains to be seen whether a more holistic EU migration and asylum approach will solve the challenges that lie ahead. After years of negotiations, the European Parliament formally adopted the EU migration and asylum policy in April 2024. It represents a coordinated approach to managing migration by addressing challenges through border control, asylum procedures and collaboration with third countries in a sustainable manner. The Common European Asylum System was reformed to establish a more efficient process, including new screening procedures and a biometric database for asylum seekers at the EU's external borders. Member states enhanced solidarity in hosting and processing asylum seekers, improving conditions for refugees. Meanwhile, cooperation with third countries aimed to address root causes of migration and facilitate returns of irregular migrants, and partnerships were strengthened with countries of origin and transit - agreements with Tunisia, Egypt, and Mauritania are meant to prevent illegal immigration before reaching the EU border.

Still, Europe remains the oldest continent worldwide with a median age of above 44 years, and represents only around 5% of the global population. To address labor shortages and attract skilled labor, the EU proposed a voluntary EU Talent Pool in 2023 to match jobseekers and vacancies across skill levels. Additionally, the Commission suggested recognizing qualifications of third-country nationals to support their integration into the labor market and simplify international recruitment processes for improved transparency in qualification recognition. EU enlargement could potentially tackle some of the EU demographic issues, but little progress is on the table. The EU has given the "EU candidate status" to nine countries (Albania, Bosnia and Herzegovina, Montenegro, North Macedonia, Serbia, Georgia, Moldova, Turkey, Ukraine) and started negotiations with six of them. In theory, AI should allow for productivity gains of 6% over the next ten years, which if fully implemented could tackle the lack of 12mn European in the labor force in 2030[5]. But the most sustainable solution would be for the EU to combine embracing AI with a rethink of the immigration strategy, as well as labor reforms to boost participation rates and become more productive and competitive.

[4] https://ec.europa.eu/commission/presscorner/detail/en/qanda_23_6045

[5] Read our report here : European labor markets: Migration matters (allianz.com)

Box 3: What needs to be done to navigate the challenges of the EU climate policy

Although the transition to clean energy appears unstoppable, it remains to be seen how prominently it will feature on the next Commission's agenda. The outgoing European Commission has made its last major climate policy initiative before the 2024 elections by publishing its Communication on a 2040 climate target. By recommending a net emissions reduction target of 90% compared to 1990 levels, it sets the strategic groundwork for the forthcoming legislative period. This marks the start of policy planning and public debate on the desired level of ambition and essential climate policy reforms leading up to 2040.

Key imminent climate issues for the new leadership include the final adoption of the Nature Restoration Law, regulation to reduce methane emissions and CO2 emission standards for heavy-duty vehicles. Although a final deal between member state governments in the Council and the Parliament on these issues has been reached, recent developments obstructing the Nature Restoration Law indicate potential challenges if the EU leadership shifts to the right, as predicted in polls. Other files, such as carbon removal certification, have yet to see a deal, and some legislation, like the Green Claims Directive, is still in earlier stages of the process. The European Green Deal has also already increased ambition legally, which will necessarily advance existing instruments, and developed new ones. These include the expansion of the Emissions Trading Scheme (ETS) to include shipping, the creation of a second trading scheme for buildings and road transport (ETS-II), and the implementation of a Carbon Border Adjustment Mechanism (CBAM) for sectors like iron and steel, aluminium, cement, fertilizer, electricity and hydrogen. These regulations include mechanisms that require additional action and adjustments to fulfil their targets.

A comprehensive framework for carbon management is also needed. Technologies for CO2 capture and subsequent utilization or storage (CCS[6], CCU[7], and CDR[8]) are crucial for achieving the interim 2040 target. Achieving desired carbon removal levels requires enormous resources, strong support for development and a single European market for CO2 transport and storage capacity. However, this could lead to new political conflicts, as seen in Germany with the sensitivity around CCS.

Future EU energy policy must better protect vulnerable citizens through well-designed mechanisms. The social dimension of climate policy is becoming increasingly important, interacting through energy prices, jobs and incentives to change. Neglecting emerging problems and social unrest will damage the reputation of climate policy in the EU and beyond. The Commission should focus on the functioning of the Social Climate Fund (SCF) and the Just Transition Fund (JTF), treating them as flagship projects and giving them due prominence.

[6] CCS refers to processes that directly capture carbon dioxide emissions from "point sources" such as fossil-fuel power plants or industrial facilities, with the carbon dioxide being stored for a long period.

[7] CCU utilizes captured carbon dioxide in secondary processes (synthetic fuels, chemicals, materials).

[8] CDR refers to processes that capture carbon dioxide from the atmosphere instead of simply reducing emissions, storing it durably on land, in the ocean, geological formations or products (i.e. concrete).

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