

Coalition Negotiations

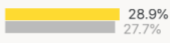

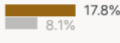








State of Play Before Really Tough Questions


Election winner loses, election loser wins

Voting and election result

Republic of Estonia

Data as of Mar 8, 2019 3:59 PM

Party or independent candidate	Votes	Percentage of votes	Mandates
Eesti Reformierakond	162363	 28.9% 27.7%	34(+4)
Eesti Keskerakond	129618	 23.1% 24.8%	26(-1)
Eesti Konservatiivne Rahvaerakond	99671	 17.8% 8.1%	19(+12)
Isamaa Erakond	64219	 11.4% 13.7%	12(-2)
Sotsiaaldemokraatlik Erakond	55175	 9.8% 15.2%	10(-5)
5% threshold: 28057.1 votes			
Erakond Eesti 200	24448	 4.4%	0
Erakond Eestimaa Rohelised	10227	 1.8% 0.9%	0(0)
Elurikkuse Erakond	6858	 1.2%	0
Eesti Vabaerakond	6461	 1.2% 8.7%	0(-8)
Independent candidates	1590	 0.3% 0.2%	0(0)
Eestimaa Ühendatud Vasakpartei	511	 0.1% 0.1%	0(0)

 Election results in 2015

Eesti Reformierakond – Estonian Reform Party (ALDE)

Eesti Keskerakond – Estonian Center Party (ALDE)

Eesti Konservatiivne Rahvaerakond – Estonian Conservative People's Party (unallied in any European family, closest to ECR)

Isamaa Erakond – Pro Patria Party (EPP)

Sotsiaaldemokraatlik Erakond – Social Democratic Party (PES)

After the election day on March 3, it seemed that the Reform Party, led by the former MEP Kaja Kallas (who won the elections, in the ALDE family) would regain power after a 2,5-year hiatus. However, the still-in-office prime minister Jüri Ratas had other plans.

On Friday March 8, Mr Ratas and his closest allies in the Centre Party (CP, also in the ALDE family) declined the offer from the Reform Party to form a coalition, citing contradictions on policy. After the weekend, on March 11, Mr Ratas announced that they will instead try to form a government together with centre-right Pro Patria (EPP) and far-right EKRE. It has become evident that the Centre Party's decision to reject Reform's offer was not in fact based on fundamental disagreements on key policy issues but rather on the CP's (and Mr Ratas') desire to remain in power.

Coalitions talks started off with easier issues

The Centre Party, Pro Patria and EKRE began coalition discussion on March 13. Their first objective was to reaffirm Estonia's foreign policy stance which included organizing an event for the foreign ambassadors. This step was taken to show that EKRE's radical rhetoric against the EU and other international organisations will not affect actual policies of the next Estonian government.

After that the parties have discussed a number of policy areas with first days focusing on areas where they had little problem in coming to an agreement (i.e. agriculture, rural policy, sport, culture and youth work).

First signs of fundamental dissonance

On the third day the parties decided, among other things, to shift more money to abortion counselling. This was a compromise on EKRE's election promise to end state-funded abortions.

While they managed to come to an agreement on the policy itself, the problems for the coalition started with EKRE's public rhetoric around the topic. This led to the prime minister and one of his closest allies to publicly apologise for EKRE's statements.

Another obvious dissonance has been on higher education where EKRE's chairman attacked a number of universities for accepting too many foreign students (thinly veiled racism) which prompted the prime minister to step in and essentially tell the media that the government's view is actually contrary to what EKRE's leader said.

EKRE's policies watered down

Almost all radical election promises of EKRE have either been rejected by the Centre Party and Pro Patria or their content has been stripped down to almost no real substance. This has happened for example on issues like abortion, immigration, value-added tax and border control.

Some key issues are still on the table – such as turning back the clock on same sex unions, which were legalized in 2014. Again the prime minister's party is expected to push back here although they could give in to something in the middle of the road – such as agreeing to analyse the constitutionality of the current set up etc, kicking the can down the road.

However, EKRE's rhetoric and public statements have largely remained the same as before the elections, while the party leaders have on numerous occasions pledged to tone down their fiery and aggressive style, with most argumentation lines coming of the Bannon playbook. This is proving to be a serious issue as the first post-election polls show the Center Party losing support, because their largely Russian speaking electorate is dumbfounded that their party has chosen to negotiate with the far-right who's take on foreigners, including the Soviet era Russian immigrants who make up 25% of the population, has been xenophobic, to say the least. According to polls, the vast majority of voters seem to support coalition options with the Reform Party in it, with the coalition between Reform and Center Party enjoying most support.

Tough questions on taxation and spending still to come

So far, the three parties have largely avoided any decisions on issues that involve significant sums of money (e.g. infrastructure, excise duties, welfare state). There have been initial discussions on those topics with an aim to understand each other's political positions but when it comes to making decisions with actual numbers behind them (e.g. whether and how much to spend on project A; whether and how much should tax B be changed), then these have been left for the upcoming week (March 25 onwards).

All this must be seen in the light of new information regarding the state budget: it has become evident that last year's structural deficit was somewhat bigger than expected, up to 1% of GDP (unconfirmed). This leaves very little room for manoeuvring as the next government would then have to balance the budget by 0,5% of GDP per year. At the same time, all 3 negotiating parties campaigned on no tax hikes.

What to expect from those tax and spend issues?

- Disagreements between the three parties will be more evident and discussions will be more stressful than they have been so far. This can lead to the collapse of the planned coalition.
- The parties have promised to not increase any taxes (some excise duties might be lowered, such as on alcohol, and also on electricity and fuel).
- They also foresee continued investments into national road infrastructure (ideally, 2+2 roads on the three major routes). The budgetary constraints mean that this can only be done with outside financing. The potential additional constraints on temporary workers and immigration are of course in contradiction with large infrastructure building – Estonia's construction sector already relies heavily on Ukrainian, Polish and Russian temporary workers, as we have been in a long boom cycle with historic lows in unemployment.
- Rail Baltica, the 5+ bln € infrastructure project in the Baltics, with most of the financing coming from the Connecting Europe Facility, has been heavily criticized by EKRE and the party has indicated this to be one of their red lines. The prime minister's party is expected to defend the project, where first investments and a lot of preparatory work has already been conducted in a 3 countries.
- Potential shake-up of the pensions system. Pro Patria's fundamental election promise was to end mandatory payments by employees to a pension fund, the so called II pillar of the Estonian pension system. From the point of view of the state, this can be also a major revenue source for the new coalition (currently all employees pay 2% of their salary into a fund chosen by themselves, with the state adding a 4% payment).

Public reaction

First post-election polling has been negative for the prime minister. The media has on balance also been critical – not only because of the far-right conservatives, but also due to the vagueness of the expected coalition treaty and the prime minister's soft handling of the process.

For the business community, the new coalition is unlikely to prove directly dangerous (through taxation or other invasive policies). The effects could be indirect, perhaps starting to hurt recruiting efforts for the already strained but booming ICT sector which is in dire need of foreign talent.

The urban and more progressive electorate is in a state of mild shock, with daily (albeit small) protests accompanying the negotiations. The base of the new coalition, if it is to be born, will be in rural areas mostly and the push back from the prime minister's party's Russian speaking voters could mean long-term changes in Estonian politics. It is obvious that the prime minister has taken a huge gamble to keep his portfolio despite losing to the Reform Party at the March 3 polls.

The document has been compiled by Meta Advisory Group OÜ. For further information on the issues covered, please contact Erki Taube via erki.taube@metaadvisory.ee or Andreas Kaju via andreas.kaju@metaadvisory.ee