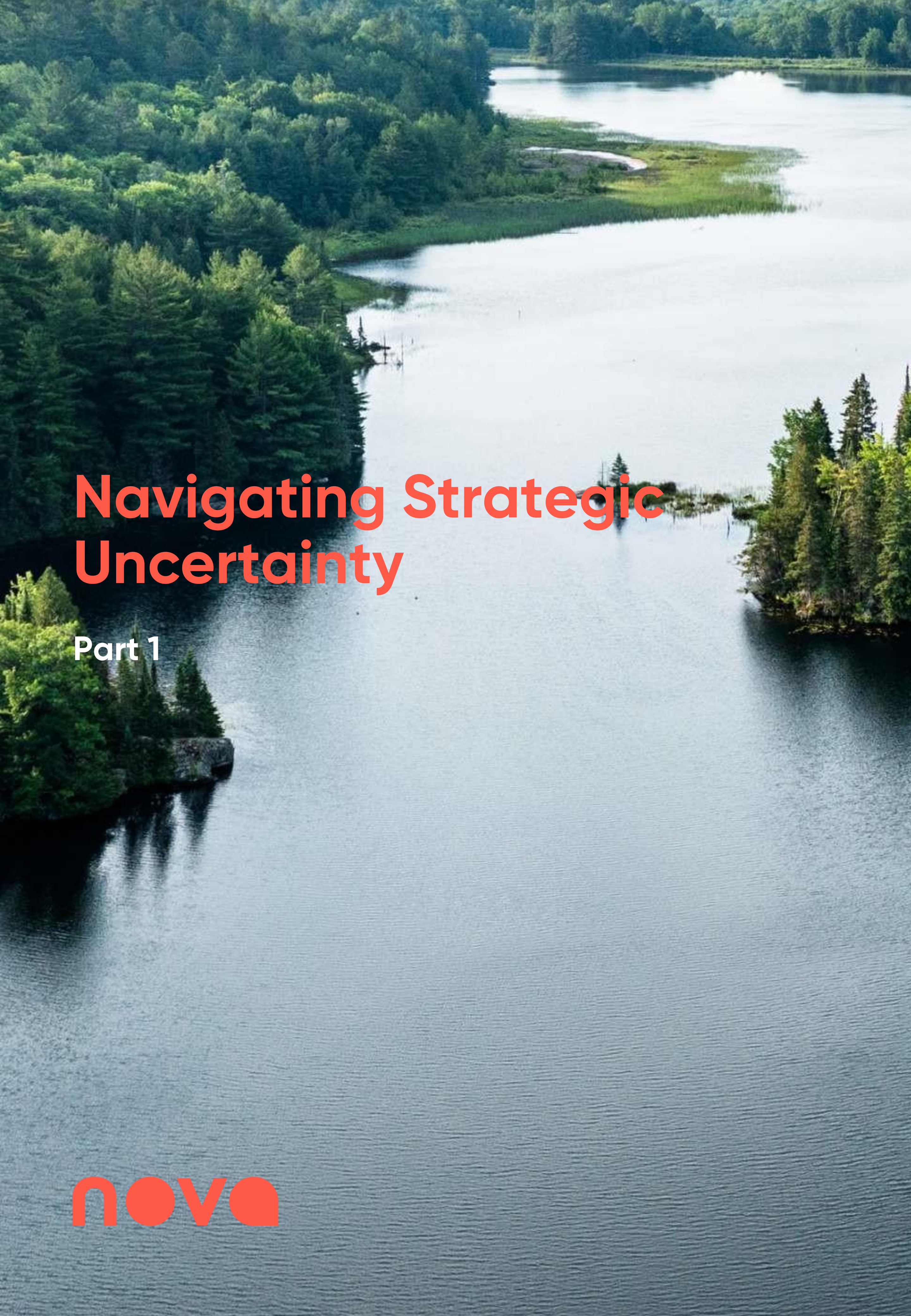

Navigating Strategic Uncertainty

Part 1

Navigating Strategic Uncertainty

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European firms are operating under increasing strain. The current geopolitical turmoil adds considerable complexity to strategic decision-making, where a multitude of variables must be factored in, and countless scenario-planning exercises seem, rather ironically, designed to never quite match reality. In these eventful times, the challenges confronting European businesses remain all too familiar: the contagion effects of the Ukraine–Russia war, a persistent loss of competitiveness, fragmented EU capital markets, subdued consumer appetite, and the looming threat of cheaper imports, particularly for industries like German automotive manufacturing, now struggling to match the efficiency gains of their Asian counterparts.

The start of 2025 has proven especially volatile, with several developments adding to an already uncertain landscape. Among the most consequential are the EU's omnibus legislation to ease sustainability reporting burdens; the continued unpredictability of the second Trump administration's policy agenda, marked by abrupt shifts in foreign relations and economic priorities; and the intensification of the conflict between Israel and Iran, which has recently seen the U.S. join Israeli offensives aimed at demolishing Iran's nuclear program (Vox, 2025). These overlapping developments have deepened the climate of legislative and geopolitical ambiguity that multinational enterprises must now navigate.

On one side of the Atlantic, the EU's ambition for sustainability is being actively rolled back. The proposed omnibus package would exempt approximately 80% of companies from the CSRD's reporting scope, introduce sweeping simplifications, and reduce compliance obligations (ESG Today, 2025). These rollbacks have raised questions about the EU's commitment to its own environmental goals and created uncertainty for firms that had already invested in compliance structures. Similarly, in the U.S., the second Trump administration has initiated a rollback of sustainability and environmental initiatives; doubling down on a fossil-fuel-first agenda (Newsweek, 2025), withdrawing from the Paris Agreement (EU Parliament, 2025), slashing subsidies for green ventures (Reuters, 2025), and reviving the "drill baby drill" rhetoric (The Guardian, 2025).

While it is clear that the Trump administration will not be a champion of sustainability, the EU's actions are not exactly sending a stronger signal either. Both major players appear to be retreating from earlier commitments, contributing to a broader atmosphere of waning institutional appetite for ESG. This erosion of momentum complicates efforts by multinational firms to formulate consistent sustainability strategies across jurisdictions.

In parallel, the Trump administration's economic playbook has disrupted the global trade order. Its transactional approach to governance has cast a long shadow over Western economic integration, fueling uncertainty for firms deeply embedded in global value chains. Tariffs, introduced as part of the administration's protectionist strategy, have heightened tensions in international trade and rattled financial markets, triggering sharp corrections across bonds, currencies, and equities (NPR, 2025).

In a separate but equally destabilizing development, the conflict between Israel and Iran has intensified, prompting the U.S. to intervene by bombing multiple nuclear development facilities in Iran (BBC, 2025). This escalation, in line with the Trump administration's emphasis on reasserting U.S. global dominance, introduces a new layer of geopolitical risk for multinational enterprises operating in or trading with the region, and amplifies the broader vulnerabilities that global value chains are increasingly exposed to.

In this volatile environment, success depends on firms' ability to make sound strategic investments, improve the accuracy of long-term forecasting, and adapt financial planning to rapidly evolving external shocks. To meet these demands, multinational enterprises are being forced to recalibrate their financial strategies — from re-evaluating capital allocation and forecasting assumptions to building up liquidity buffers that can offset rising costs associated with trade barriers (FT, 2025).

The

Academic Perspective: Understanding the Business Impact of Uncertainty

To better understand how firms might navigate this evolving landscape, we turn to academic literature, which offers valuable insight into the complex relationship between policy uncertainty, investment behavior, and innovation.

The Economic Policy Uncertainty Index developed by Baker, Bloom and Davis (2016) shows that global economies entered 2025 navigating the highest recorded levels of political uncertainty, for the first time surpassing the 500 mark and showing a sharp increase relative to 2024 figures.

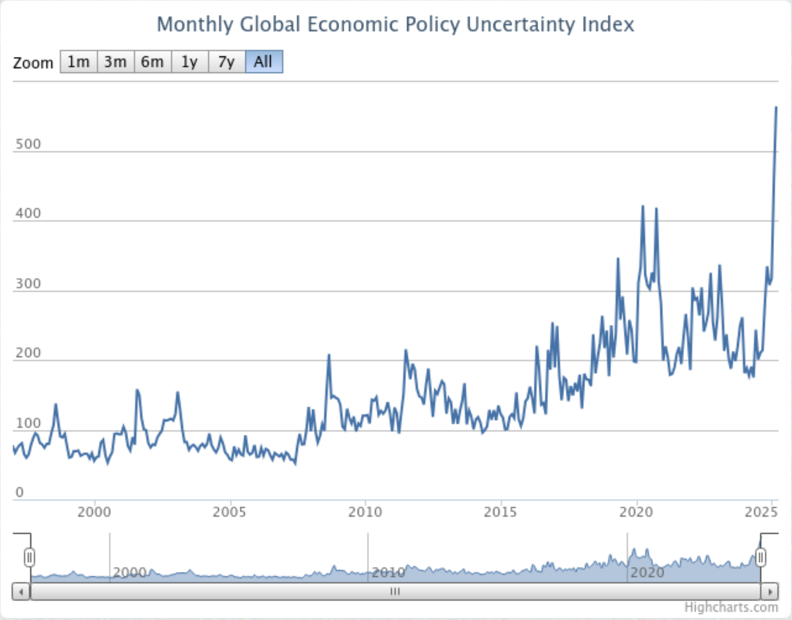

Chart 1. Economic Policy Uncertainty Index retrieved from www.policyuncertainty.com

Since firms operate, and will continue to, under the jurisdiction of real-world governments, it is no surprise that such levels of political instability and regulatory ambiguity frequently disrupt corporate operations. Scholars have long explored this relationship. Xu (2019), for instance, finds that uncertainty raises firms' cost of capital, leading to reduced investment in innovation, particularly among financially constrained firms and those reliant on external finance. These characteristics are often found in small and high-growth enterprises, making them especially vulnerable (Hill et al., 2018).

Financial markets introduce further complications. Gilchrist and Zakrajsek (2007) observe that fluctuations in bond prices influence corporate capital expenditures, while Pastor and Veronesi (2012, 2013) demonstrate that undiversifiable political risk drives up the equity risk premium. This leads to a more expensive financing mix, as firms face higher costs of equity and increasingly rely on debt.

Despite these headwinds, not all academic evidence paints a negative picture. Zhang et al. (2024) argue that innovation remains a cornerstone of long-term value creation, and many firms continue to pursue it even during uncertain times. Ross et al. (2018) suggest that policy uncertainty can stimulate investment when companies identify overlooked opportunities. Du et al. (2023) add that uncertainty may trigger both incentive and choice effects, prompting firms to boost R&D spending and reinvest resulting gains into further innovation, creating a self-reinforcing cycle of progress. These findings align with Chatjuthamard et al. (2020), who contend that some firms achieve superior growth under heightened policy uncertainty.

There are also transparency-related benefits. Qian et al. (2025) find that elevated economic policy uncertainty increases voluntary information disclosure, both internally and externally, as firms seek to maintain market confidence and access to capital. Ge and Zhang (2025) reinforce this view, showing that transparency improves the accuracy of forecasting. Internal transparency, in particular, has been linked to improved responsiveness and adaptability (Williams et al., 2013), enhanced sense-making (Swink & Schoenherr, 2015), and, as a result of these combined benefits, more effective decision-making under pressure.

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