

Explanatory and background note, European Council

We all have a responsibility to ensure that our Union is stronger, more innovative, and productive, and to ensure that sustainability supports the economy and jobs while safeguarding our planet.

I. Competitiveness

The EU has a [competitiveness problem](#), but also opportunities to [improve competitiveness](#). (these are two seven-page summaries of competitiveness, policies, and the Letto and Draghi reports)

The EU is lagging in strategic sectors, in part because the US and China are subsidizing them, and our state-aid and competition rules, in place to ensure a competitive and rules-based marketplace, may need refinement to meet the challenges in a world where competitors increasingly apply protectionism, and realpolitik and geo-economics increasingly dominate. Mario Draghi's report states that Europe needs to invest up to €800bn per year to boost innovation, increase productivity, pay for the Green transition, and meet Europe's expanding defense needs, in light of Russia's invasion of Ukraine. We need painful reforms, a move away from dependencies on critical raw materials from China, and the securing of important supply chains.

Industrial policy: The EU needs to support actions by the Commission to counter subsidies and protectionist measures in major competitors while supporting new proposals to strengthen innovation, economic growth, industrial champions, development, new technologies, and sustainability. The [innovation fund](#) is a start. The International Energy Agency (IEA) estimates that around 90 % of mass manufacturing capacity for several key clean energy technologies is located in China and the Asia-Pacific region. During the last mandate, EU has supported [breakthrough technologies](#) and allowed state aid under [the IPCEI](#) and legislators have adopted a number of specific regulatory frameworks targeting key industries in the net-zero industrial age. These concern batteries, semiconductors ('Chips Act') and critical raw materials (CRMS - 'CRMs Act'), and support the production of strategic technologies (Net-zero Industry Act - NZIA) and a strategic technologies for Europe platform – STEP). Regarding chips, for example, the Commission recently stressed that the launch of the European Chips Act had already attracted public and private investment commitments of €115 billion.

There needs to be greater defense collaboration, research and development across national borders, and more joint procurement. Our goal is 35% joint procurement, we are at 18%, which means lots of waste (overlap and duplication). Currently, five different types of howitzers are manufactured in Europe, whereas the US produces only one. There are twelve European types of battle tanks, while in the US there is only one. As for the fighter jets, the Eurofighter, Rafale and Gripen represent only one-third of the total European fleet, with US fighter jets comprising the rest. Finally, in defense shipbuilding, the largest program in Europe constructs only 14% of its fleet. The EU's investment in defense research and innovation is much lower than that of its industrial competitors. We also need to purchase more EU made equipment, and ensure it is interoperable. 2022-23, 78% of EU countries' procurement spending was diverted to purchases from suppliers located outside the EU, including 63% based in the US.

The transatlantic relationship is the deepest and most extensive in the world. The mutual investment stock is 8.5 trillion Euros, and transatlantic commercial ties support at least 16 million jobs on both sides of the Atlantic – many of them service what amounts to half of the world’s personal consumption. Trade is over 2bn Euros daily, with 65% of trade being intra-firm; firms that face similar discrimination and unfair trade practices in China.¹ This means the EU has every incentive to work with our transatlantic partners to ensure that industrial policies, sustainability and defense policies are supportive and productive, rather than destructive. This of course is contingent on a collaborative and cooperative American approach, where partners and allies are not discriminated against.

The automotive industry directly and indirectly employs 7% of EU workers, and is severely challenged by Chinese EVs, US and Chinese competition, domestic subsidies, and bilateral trade disputes. China has also retaliated against EU tariffs on imported Chinese EVs. The US has imposed a 100% tariff on Chinese electric vehicles, and we have imposed 27.5-47% tariffs on different Chinese firms’ EVs after a WTO-compatible investigation into illegal subsidies from the Chinese government. However, the EU levels are still low enough that some Chinese firms can export EVs at a profit to the EU market, and several firms are investing in select EU markets to build EVs in the EU. At the same time, the automobile market is dependent on Chinese raw materials and EV batteries, and China has retaliated by imposing tariffs on select EU goods, including French cognac. The US is also providing billions in support to attract firms to invest and build factories in the US through the Inflation Reduction Act. How do we counter the dumping of Chinese EVs in Europe and US subsidies, adhere to our long-term net-zero emissions goal, and ensure the EU has an automotive industry?

If the incoming US administration imposes tariffs across the board on EU exports, how should we respond politically? Which areas of goods and services should we target or exempt? Should we purchase more LNG from the US? 48% of European [liquefied natural gas came](#) from the US in 2024; we can increase that, especially since we are banning Russian oil and gas from 2027. The Commission has a list of areas and sectors to hit back at the US, but what are the geopolitical concerns and the repercussions on our economies? We need to safeguard our industries and our continent’s security. When the US and China had a trade war in 2018-2019 it cost us roughly 1% of our GDP, and if we face 10-120 % tariffs on our exports to the US, EU countries will face a €150 billion annual loss of exports to the US. China may also dump products into our market, forcing us to act. The EU supports a multilateral trading system based on rules, but the World Trade Organization’s judicial arm is in limbo, with no appeals process since 2020, and no compromise in sight.

II. Ukraine

We need to discuss unity in [purpose regarding NATO](#) and, building on the discussion of competitiveness in the defense industry, how to better coordinate and cooperate on defense policy, increased spending and procurement, in order to safeguard Europe. [EDIRPA](#) (the joint defense procurement instrument) ends in 2025, and any joint armaments procurement is subject to a Member State’s approval. The EU lacks any kind of permanent defense

¹ Sources: IMF, Eurostat, Transatlantic Economy 2024.

procurement instrument. Expanding joint armaments procurement also creates EU jobs if the armaments are ordered from EU firms. This is what the US does when it expands arms support. US support for Ukraine has resulted in years of orders for US firms. Russia's war on Ukraine has laid bare the challenges the European defense industry faces as it tries to meet increased demand and ramp up production in the wake of a fundamentally changed security environment in Europe. The European defense industry comprises a number of large multinational companies, mid-caps and over 2 000 small and medium-sized enterprises. It faces a multitude of challenges: decades of under-investment, fragmentation, lack of critical raw materials and semiconductors, and insufficient manufacturing capability. We can discuss a larger joint defense fund, one exempt from budget rules.

We should expand the [European Peace Facility](#) beyond its [current funding](#). In February 2024 the European Council agreed on the Commission's proposal to provide Ukraine with regular and predictable financial support between now and 2027. Under the so-called "[Ukraine Facility](#)", the Commission will make available for Ukraine up to €50 billion in [grants and highly concessional loans](#). This crucial funding will help Ukraine keep its administration running, pay salaries, pensions, and provide basic public services, as it continues to defend itself against Russia's aggression. In October 2024, the EU and G7 partners agreed to collectively provide loans of \$50 billion to support Ukraine's urgent budgetary, military and reconstruction needs, financed by extraordinary revenues from immobilized Russian sovereign assets. The EU will contribute with \$20 billion. On November 9, 2024, Josep Borrell said the EU's [support is unwavering](#). We need to do more. The Commission is proposing that states can use [Cohesion Funds for expenses that support defense and the defense industries](#). How can we approach the US to coordinate US and EU foreign and security policies and to avoid unilateral decisions without consultations such as on relations with China, the issue of Taiwan, sanctions on Russia, and economic and military support for Russia. The Draghi report strongly advocates accelerating technological and scientific innovation and a genuine 'foreign economic policy' to increase security and reduce critical dependencies.

III. Climate leadership

The EU has done much on climate, but some Member States think it is time other countries and regions to more, and that the EU is doing enough. The US is also dropping certain targets for climate policy. The State of the Energy Union 2024 report finds the EU has withstood critical risks to its security of energy supply, regained control over the energy market and prices, and accelerated the transition towards climate neutrality. The EU has successfully put in place the necessary regulatory and financing framework to achieve its 2030 climate and energy goals and lay the foundations for renewed economic growth and competitiveness. However, cost increases and other countries' actions (or inactions) remind us of the precariousness of our situation. The recent floods in continental Europe and Spain have also reminded us of the immanency of climate change and the need for resilience. We cannot reduce our efforts to create a sustainable environment. The deployment of energy-efficient, net-zero and low-carbon solutions will be needed, and we need to consider how these technologies can be made in Europe.

The EU has banned all Russian oil and gas imports from 2027 and aims to create sustainable, competitive, affordable energy sources. This has already led to substantial reductions in energy use and efficiency in Europe, but much more is needed, and this requires innovation and joint commitments. Energy prices are already 2-5 times higher than in China and the US, and this is not good for EU firms and competitiveness.

The EU has opportunities at hand to lead the innovation of clean technologies. But we need better synergies. EV batteries for electric vehicles can rely on a strong automotive industry for positive spillovers, and the offshore wind sector on the EU's oil and gas industry. Furthermore, the solar PV and heat pump sectors can learn and exploit synergies with the building industry. We recognize that a well-planned green transition and energy security are not only complementary imperatives but can also present our economies with significant opportunities to achieve both our competitiveness and decarbonization objectives by leveraging inexpensive, sustainable energy and reducing dependence on external sources. We need to discuss whether the plastics treaty that is being negotiated can be pursued without the US.