Institute for European
Analysis and Policy

Hub for New Industrial Policy
& Economic Governance

LUHNIP Monthly brief on EU Industrial Policy
February 2024

Dimitri Zurstrassen and Donato Di Carlo

LUISS

LUHNIP Monthly brief on EU Industrial Policy

February 2024

Dimitri Zurstrassen and Donato Di Carlo

Every month, our Monthly Brief on EU industrial policy provides a bullet-point recap of the month's main events, followed by three reasoned deep dives into significant developments in EU industrial policy. Our analysis is complemented by a monthly guest contribution from renowned experts or practitioners in the field.

***

Last Month in Brief

- **1 February:** The European Parliament and the Council of the EU reach a provisional agreement on the Single Market Emergency Instrument (SMEI).
- **6 February:** The European Parliament and the Council of the EU reach a provisional agreement on the Net-Zero Industry Act (NZIA) (**see Deep Dive 1**).
- **8-9 February:** European ministers responsible for Internal market and Industry meet in Genk (Belgium) for an informal meeting to discuss strengthening the competitiveness of European industry (**on this issue see our guest contribution**).
- **14-15 February:** European ministers for Research and Innovation meet in La Hulpe (Belgium) for an informal meeting to discuss, among other topics, the decarbonisation of European industry and the strengthening of EU competitiveness (**on this issue see our guest contribution**).
- **16 February:** The European Commission opens an in-depth investigation under the Foreign Subsidies Regulation regarding a public procurement offer from CRRC Quingdao Sifgang Locomotive Co. Ltd (**see Deep Dive 2**).
- **23-24 February:** European finance ministers meet in Ghent (Belgium) to discuss initiatives to deepen the Capital Markets Union and issues of economic competitiveness (**on this issue see our guest contribution**).
- **24 February:** The European Commission opens formal proceedings against TikTok under the Digital Services Act on Monday, due to possible breaches in several areas, including child protection.
- **25-29 February:** European ministers responsible for trade meet in Abu Dhabi (UAE) at the margins of the 13th WTO ministerial conference to approve its conclusions (**see Deep Dive 3**).
- **27 February:** The European Commission adopts a communication on Advanced Materials for industrial leadership.

LUHNIP's Deep Dives

1) The Council of the EU/European Parliament agreement on the Net-Zero Industry Act (NZIA)

On 6 February 2024, the negotiators of the European Parliament and the Council of the EU reached an agreement on the Net-Zero Industry Act (NZIA). One week later, on 16 February, the COREPER approved the agreement. Then, the European Parliament's Committee on Industry, Research and Energy (ITRE) validated it on 22 February. From the procedural viewpoint, the last missing step is the final approval by the European Parliament during its April plenary session.

Looking at the differences between this agreement and the position adopted by the European Parliament in November 2023, two key elements can be underlined. The first difference concerns the approved list of net-zero technologies. The agreement between the two institutions lays down a single list, while the EP's position foresaw two lists: a list of zero-net technologies and a list of strategic technologies. According to the Council's position, the goal of this single list is to provide certainty for investors on which technologies can benefit from the permit fast tracks set by the regulation. Member States maintain complete autonomy when choosing the technologies to invest in, as asked by the S&D group within the EP and lobbied by some Member States.

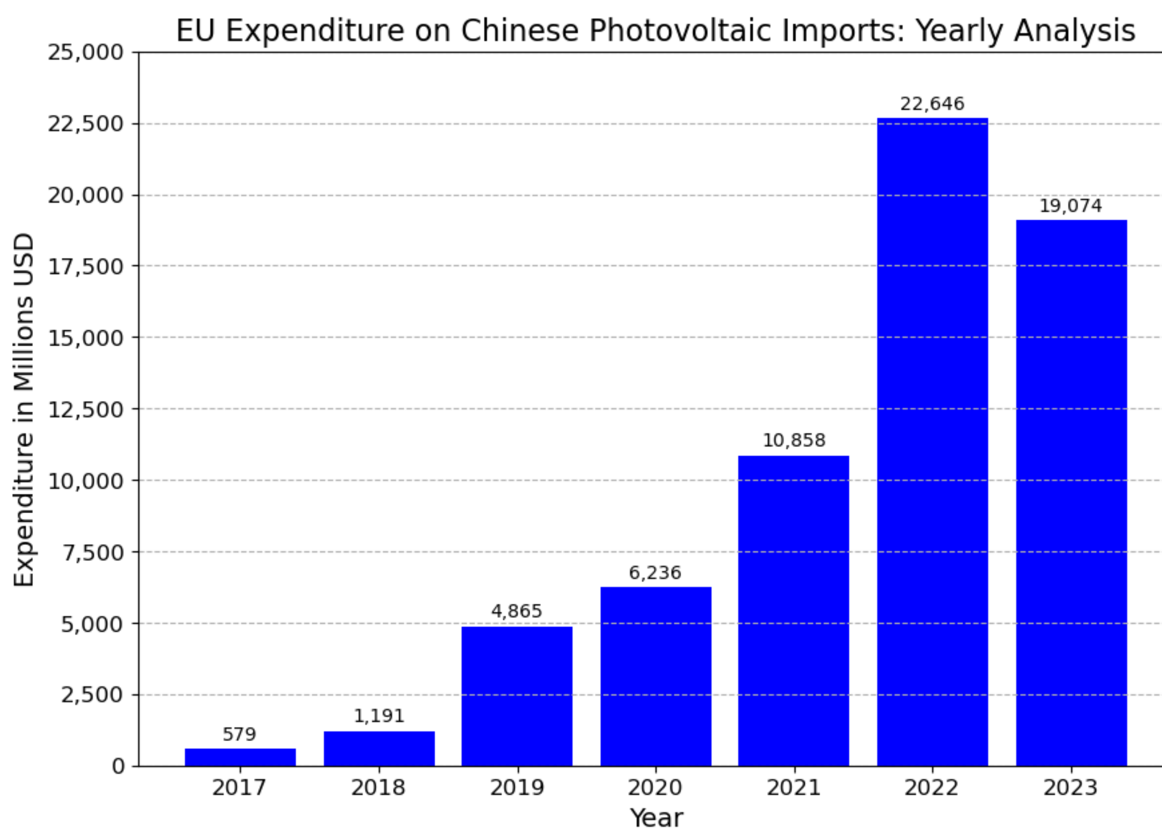
The second difference concerns the duration of the permit-granting process. The EP-Council agreement slightly increases the necessary number of months. This increase is probably due to Member States' push to not set bureaucratic timings, which would be difficult to respect. The result is that for the net-zero technology manufacturing projects with a yearly manufacturing capacity of less than 1 gigawatt (GW), the agreement establishes that the permit-granting process shall not exceed 12 months, instead of the 9 asked by the EP. Moreover, for the category of net-zero technology manufacturing projects, with a yearly manufacturing capacity of 1 GW or more, the time limit set is 18 months, instead of the 12 proposed by the EP.

Also, there are differences concerning the criteria for selection of net-zero investment projects and the rules on public procurement. Among these criteria, there is one which foresees that the project has to strengthen the manufacturing capacity of a component or a segment of the net-zero technology supply chain by adding manufacturing capacity in the EU for a net-zero technology, for which the Union depends for more than 50% on imports coming from third countries. When it comes to public procurement, a so-called resilience contribution is applied: the proportion of technologies or components coming from a third country must not exceed 50%. Finally, the agreement foresees that Member States can designate Net-Zero Industry Valleys which can enjoy easier permitting procedures. The designation of Net-Zero Industry Valleys was promoted by the European Parliament which strongly lobbied for it.

LUHNIP's take

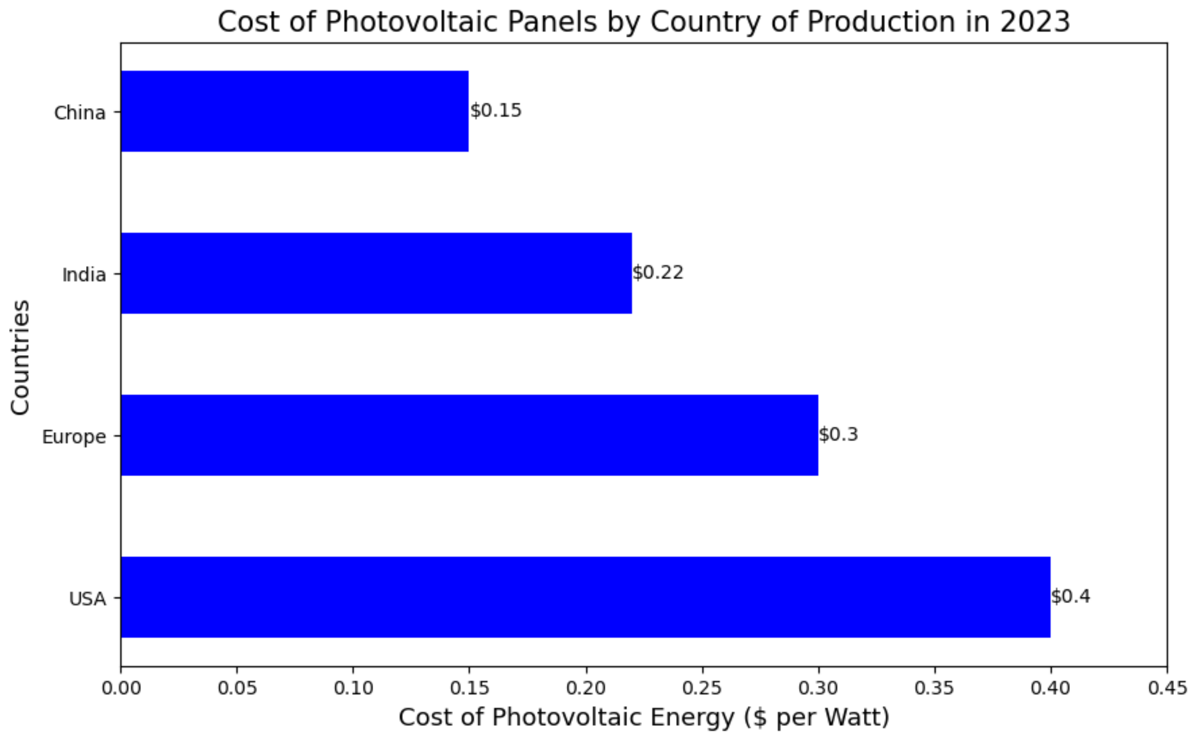
The agreement between the Council of the European Union and the European Parliament on the Net-Zero Industry Act is the culmination of a long process of amending the Commission's proposal of March 2023. The adoption of the flagship text of the Green Deal Industrial Plan, should, according to the European Commission, enable the European Union to respond to the challenges posed by the application of the US Inflation Reduction Act (IRA) and increasing Chinese competition in strategic industries to reach environmental targets. The case of solar panels, for which the EU has increased its share of imports from China in the last years (**see Graph 1**), is emblematic of this increasing Chinese competition and the pressure exerted by producers on the Commission to take action to prevent production structures from relocating outside the EU. This increase is particularly due to their low cost compared to the European ones, as we can observe from **Graph 2,** as a result of manufacturing overproduction in China. If no urgent measures are taken by the EU institutions, the bloc is in danger of failing to meet its 40% target for increasing domestic capacity in this sector within the decade, as **Graph 3** shows.

Graph 1: Evolution of EU expenditure on Chinese Photovoltaic imports from 2017 to 2023 (in millions USD)



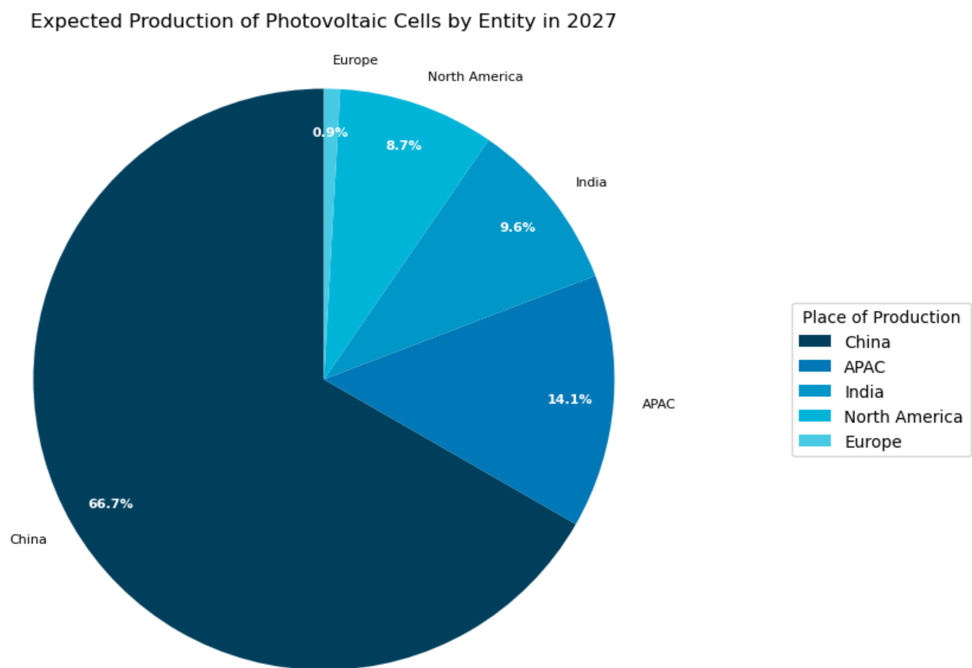
Source: Our elaboration based on Wood Mackenzie data.

Graph 2: Cost of photovoltaic panel by country of production in 2023



Source: Our elaboration based on Ember data.

Graph 3: Expected production of Photovoltaic cells by entity in 2027



Source: Our elaboration based on IEA data.

However, after months of negotiations, we can observe that the final text of the Net-Zero Industry Act lacks the intervention and financial instruments that could make the regulation a sufficient response equal to the challenges of increasing Chinese and US competition. If the fact that the agreement lays down a single list of strategic technologies is positive, the decision to give Member States autonomy in their choices of investment in technologies risks leading to the development of national competitive strategies in this area, and therefore to failure to achieve the production objectives set in the NZIA. Also, the decision to set ambitious non-binding targets for increasing European industrial capacity without giving the industry political incentives other than administrative simplification may mean that European companies prefer to invest in other countries where they can benefit from more favourable incentives, such as the United States. Finally, there is no mention in the final text of the availability of Member States to grant financial resources other than those allocated to the Strategic Technologies for Europe Platform (STEP) at the last two European Councils (€1,5 billion). This sum is considered by experts to be insufficient to meet the EU environmental transition objectives.

2) The opening of an investigation on CRRC under the Foreign Subsidies Regulation

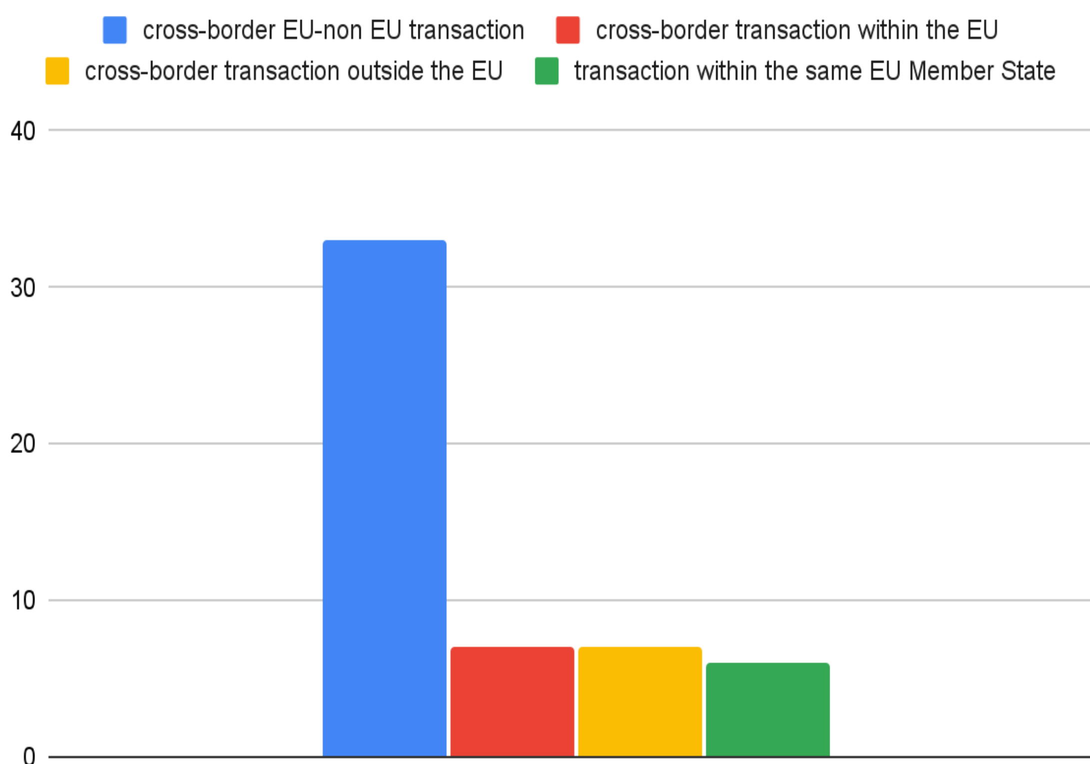
On 16 February 2024, the European Commission launched an in-depth investigation into a subsidy granted to CRRC Qingdao Sifang Locomotive Co. Ltd., a subsidiary of CRRC (China Railway Rolling Stock Corporation), a Chinese state-owned train manufacturer, in the framework of a public procurement procedure launched by Bulgaria's Ministry of Transport and Communications, relating to the provision of several electric "push-pull" trains, as well as related maintenance and staff training services. This in-depth investigation is the first one to be carried out under the EU Foreign Subsidies Regulation (FSR), which came into force on 12 July 2023. According to the European Commission, the launch of an in-depth investigation was justified by the fact that there was sufficient evidence that the company received in the three years prior to notification of the participation in the public procurement tender at least €4 million in subsidies from China.

CRRC's participation in the public tender launched by the Bulgarian Ministry of Transport and Communications is a further step in its strategy to conquer European markets. Since the creation of CRRC in June 2015 following the merger between two Chinese companies, CNR (China Northern Rolling Stock Corporation) and CSR (China Southern Rolling Stock Corporation), the world's leading producer of railway equipment focused its strategy on expanding to Chinese, African and Asian markets, but also on progressively entering the European market. In December 2015, it created a European subsidiary, CRRC ZELC Verkehrstechnik GmbH based in Vienna, to invest in the continent. For example, it took part in the EMU project signed with Czech private operator Leo Express in 2016 or in the shunting locomotives projects in Hamburg and Berlin ("Kleinstlok HH" and "AZ Lok" projects, in collaboration with Deutsche Bahn in 2017).

LUHNIP's take

The opening of an investigation on Chinese industrial champion CRRC under the Foreign Subsidies Regulation is an important step in the European Commission's strategy to combat unfair Chinese competition. It demonstrates the Commission's determination to act swiftly against the unfair Chinese government's funding of its state-owned enterprises in the railway sector, 5 years after the prohibition of the Alstom-Siemens merger, which was criticised by the French and German governments for preventing the creation of a European champion to face competition from CRRC. The question remains as to the outcome of the investigation, that is, what type of sanctions the Commission will put in place if the investigation proves that there was unfair competition. Finally, we may also wonder whether the CRRC case will be the first in a long series of investigations into Chinese subsidies, given the Commission's tougher stance on unfair Chinese competition since October 2023 and the large number of cases notified under the FSR since the start of the application of the notification obligation (**see Graph 4**).

Graph 4: Overview of the cases notified under the FSR since the start of the the application of the notification obligation (21 Oct 23-20 January 24)



Source: Our elaboration based on European Commission data.

3) The results of the 13th WTO ministerial conference

The 13th WTO Ministerial Conference was held in Abu Dhabi from 26 February to 2 March 2024. It was an occasion to renew the negotiations among its members on a significant number of different subjects such as agriculture, fishery subsidies, WTO dispute settlement reform, intellectual property issues related to COVID-19 diagnostic tools and treatments, and e-commerce.

In the current period of high geopolitical tensions (the war in Ukraine, the Israel-Palestian conflict, etc.) the main expected result was the reform of the WTO dispute settlement system. Since 2019, its activity has been blocked due to the US Administration's refusal to appoint WTO Appellate Body judges. In October 2023, it is estimated that around 30 appeals would be blocked because of this legal limbo. Concerning the WTO dispute settlement reform, the first confidential draft was shared with the organisation's members in October 2023. In addition to the need of a well-functioning appeal body, other proposals were made in order to simplify the actual procedure, but also to promote transparency and accountability. Even if this proposal found a large consensus, the WTO members could not agree on a text, mainly because of US opposition.

The 13th Ministerial Conference was also an occasion to discuss the need for a revision of the rules on industrial subsidies, a priority for the EU in the current context of proliferation of discriminatory national measures. During the negotiations, however, no sort of agreement was found on this issue and the subject was not included in the conclusions of the conference due to the opposition of India, South Africa and Indonesia. These countries argued that the granting of industrial subsidies was a national competence and that controlling them could weaken their industrial growth.

LUHNIP's take

The results of the latest WTO conference show the difficulty of finding a multilateral solution to prevent the current expansion of interventionist industrial policies around the world from leading to major market distortions. The lack of agreement on reforming the Dispute Settlement System and on the revision of industrial subsidies means that economic powers such as China and the US can pursue in the following months unilateral industrial strategies without hindrance. Despite progress on the reform of the Dispute Settlement System and the commitment made at the end of the conference to "have a full and well-functioning dispute settlement system by 2024", it seems nevertheless difficult that any breakthrough on this issue will happen before the US elections in November because of its political sensitivity in the country.

Guest contribution

Pier Carlo Padoan, Leap, Luiss University, Rome
Paolo Guerrieri, Leap, Luiss University, Rome and PSIA, Sciences Po, Paris

Industrial policy and consolidating the openness of the European economy

The new global environment and the growing influence of geopolitical factors have created new challenges for the European Union and European countries, requiring first and foremost the relaunch of EU industrial and technology policies. It must turn the environmental transition into a new engine of growth and respond to the challenges posed by other major countries, in particular the United States and China.

European industrial policy must not mean that the EU becomes more closed to the world. On the contrary, by strengthening its industrial and technological capacity, the EU must do everything in its power to protect and reform the international economic order and prevent the world from fragmenting. A world divided into two blocs or disorderly economic fragmentation would severely damage and marginalize European economies. Openness and international cooperation will remain essential for European growth.

European industrial policies, however, risk coming into conflict with those of other countries engaged in equally ambitious and largely competing processes of environmental and industrial transformation, as has already happened with the US Inflation Reduction Act (IRA).

Some observers argue that none of this will lead to conflict between countries. Their basic hypothesis is that incentives and subsidies will ultimately help not only the country that provides them, but also other countries in the fight against climate change. Unfortunately, things are not that simple. As the extensive theoretical and empirical literature has argued for some time, climate change policies are part of the so-called strategic industrial and trade policies and pose classic "collective action" problems. As we argue in our recent book,* far from helping governments to develop green technologies and diversify their supply chains, these policies could end up jeopardizing the achievement of their objectives. Coordination and cooperation agreements between countries are needed to avoid this.

The European Union and its Member States must therefore avoid any illusory approach under the banner of "Europe First", a short-sighted and ultimately self-defeating strategy, and recognize the benefits of an industrial policy that openly acknowledges the need for coordination with other countries. International coordination is more important when one looks to the near future, when the ecological transition will entail industrial restructuring on an increasingly large scale and pose complex domestic problems of political, economic, and social governance in every advanced country.

To be sure, proposing international cooperation agreements is highly problematic today, given the fragmented and conflict-ridden state of international economic relations. Cooperative solutions at the global level are also complicated by the intertwining of economic and security issues, which increases the tendency of countries to pursue conflict rather than cooperation. This is undoubtedly a great and difficult challenge, but it should lead Europe to try to prevent potential conflicts and to take the lead in coordinating its interventions - first with the other G7 countries and then extended to other interested countries. This would involve establishing common rules and limits to make the same subsidies and incentives compatible and acceptable to all. Such cooperation will become all the more necessary as government intervention in industry becomes more widespread and contributes significantly to reducing emissions, promoting new technologies and ensuring national security conditions between now and the end of the decade.

*Paolo Guerrieri and Pier Carlo Padoan, *Europa sovrana. Le tre sfide di un mondo nuovo*, Laterza, aprile 2024.