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"European competitiveness and strategic autonomy"

The European Union and the double challenge: strengthening competitiveness and enhancing economic security

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1. Introduction

The European Commission released its latest package of economic security measures at the end of January 2024 (European Commission, 2024). It includes a broad range of initiatives: enhancing screening for inbound and outbound investments, controlling sensitive exports, and increasing research funding for dual-use technology. The package implements and further develops the European Economic Security Strategy launched in June 2023 (European Commission, 2023). The objective is to foster growth, defend the EU against unfair trade practices, and collaborate with allies, aligning it with the principles of "promoting, protecting, and partnering".

The European Commission's recent release of measures underscores the increasing importance of economic security in the EU's agenda, particularly in light of political tensions and global economic shifts like the Russian invasion of Ukraine. In addition, the new global context poses significant challenges to the EU's long-term economic competitiveness. Europe has been one of the largest beneficiaries of the intense globalization in recent decades, relying on a growth model based on cheap imported energy, medium- and low-tech industries, and net exports to the rest of the world, especially China. The ongoing reconfiguration of the global economy, driven by rising energy prices, fragmentation of the global trade regime, and the emergence of new technological digital clusters, has rendered this traditional growth model unsustainable. To regain competitiveness, Europe's productive supply needs radical restructuring and reconversion (Guerrieri and Padoan, 2024).

Europe therefore faces a twofold challenge in this turbulent world: strengthening competitiveness while enhancing economic security. A greener and more competitive Union can indeed provide an effective response to make the EU more resilient and secure. But it is a complex task that requires a series of highly complex initiatives and policies, both domestically and internationally, with a lot of trade-offs between promoting growth and reducing risk. As will be argued in this paper, this dual challenge must form the basis of Europe's so-called open strategic autonomy (OSA), a concept that has long been debated in Europe and has played a central role in defining the strategies of the von der Leyen Commission in recent years (Steinberg and Wolff, 2023). The concept emphasizes the need for Europe to become a stronger player in the geopolitical arena while maintaining an open and competitive market economy. OSA integrates 'national' security considerations into EU economic policy, akin to approaches taken in the US and Japan. The fact is that you can't separate the agenda of economic security from that of European competitiveness, as done in the past. The EU has taken some steps in this direction. But much more needs to be done.

This paper delves into the multifaceted dimensions of OSA (Section 2), analyzing vulnerabilities and strengths of the EU in competitiveness and economic security, and proposing policy solutions. It explores the challenges to Europe in the ecological transition (Section 3), industrial strategies, technological policy (Sections 4 and 5), economic security measures (Section 6), and the EU's international role and relations with the Global South (Section 7). These challenges characterize the current global scenario and have relevant spillover effects on the EU economy. The last part of the paper (Section 8) points out that achieving OSA and the twin goals of enhancing economic security and competitiveness requires deepening European integration, providing EU governance with more effective policy tools and increasing financial resources at the European level.

2. The concept of strategic autonomy

The term "strategic autonomy" first emerged over a decade ago in the context of European security and defense issues (Tocci, 2021). However, its usage later shifted towards European economic matters, such as ensuring the security of supply chains and fostering technological sovereignty. This shift was prompted by a series of events and crises that characterized the international scene over the past decade, including the rise of China under Xi Jinping, Trump's protectionist policies, the COVID-19 pandemic, and more recently, energy shocks and the invasion of Ukraine.

And it is with reference to its economic aspects that this paper analyzes EU strategic autonomy. It will highlight how in Europe the concept has often been defined as "open strategic autonomy," (OSA) stressing the need for a delicate balance between safeguarding European strategic assets and the imperative of maintaining the EU's economic openness and integration with international markets (European Commission, 2021).

The precise definition and scope of strategic autonomy have been subjects of many debates and different interpretation across Europe (Tamma, 2020; Meunier & Nicolaidis, 2019; Schmitz & Seidl, 2023; Lavery, 2023; Wigger, 2023). Differing national interests and strategies among Member States have led to varying interpretations of how to make the Union an autonomous economic actor. Some have limited the concept to the EU's international dimension and initiatives, while others have emphasized - and we share this perspective - the peculiar combination of domestic and international components that define the concept of OSA.

In June 2023, the Commission published its "Economic Security Strategy and Strategic Autonomy" document, focusing on promoting competitiveness, protecting citizens, forging partnerships, and providing general guidelines to inform Member States' choices and policies (European Commission, 2023). More recently, by the end of January, the Commission – as already noted - published its second package of economic security measures (European Commission, 2024).

The heightened attention to the concept of strategic autonomy is a response to the new phase of geopolitical rivalry shaping international economic relations. In this context, the balance of power between countries, particularly the clash between the US and China, takes precedence over multilateral rules and institutions (Lake, 2021). Uncertainty and risk increasingly influence economic life, with interdependence becoming a source of both opportunity and vulnerability, often referred to as "weaponized interdependence"(Farrell and Newman, 2019). Consequently, the traditional concept of national security is evolving to include economic security.

This new world has created difficult challenges for the EU, whose institutions were designed to operate in a rules-based world. The EU was not set up to be a geopolitical body and to take any kind of significant geopolitical decision. It has to build consensus among 27 Member States with different interests. That is a very special task. Unlike the US and China, foreign and security policy within the EU largely remains the prerogative of Member States (Zuleeg, 2023). Over the past decades, the EU's economic activities and organization have operated independently of geopolitical and security considerations. Economic security and geopolitics were thus far removed from the "four freedoms" (free movement of goods, services, people, and capital) that have characterized how the European economy has functioned for decades. However, this detachment is no longer sustainable. The EU must now navigate a global context marked by major power competition while ensuring its own security through economic means, necessitating the integration of economic and geopolitical decision-making processes (Guerrieri and Padoan, 2024).

Awareness of this challenge is growing in Europe, yet the EU remains relatively unprepared for a world of geopolitics and great power competition. This vulnerability is compounded by the loss of competitiveness suffered by Europe vis-à-vis the US, China, and other advanced countries. And it is particularly serious because the geopolitical risks are real, and it would cost a great deal to get caught unprepared. In the following sections, we will analyze these vulnerabilities, beginning with Europe's greatest challenge: the ecological transition and the Green Deal.

3. The Green Deal and the new growth strategy

Vladimir Putin's decision to invade Ukraine in February 2022 significantly impacted Europe, particularly economically, revealing its overreliance on Russian energy supplies and highlighting the close connection between energy supply security and the ecological transition. This invasion demonstrated that energy dependence can be exploited as a weapon.

Europe's response was swift and effective. The EU reduced its direct imports of Russian gas from over 20 percent of total gas imports in 2020 to about 5 percent by the first half of 2023, while increasing imports of liquefied gas from the United States and Norway.

In the medium-long term, the EU's strategy revolves around the Green Deal, which aims to achieve carbon neutrality by 2050 and position the EU as the world's leading hub for zero-carbon and digital technology innovation and manufacturing (European Commission, 2023 a). A key aspect of this strategy is reducing Europe's excessive energy dependence by significantly decreasing the use of fossil fuels and prioritizing the development of renewable energy sources.

Economically, the Green Deal is envisioned as a strategy for sustainable growth. The transition to a green economy offers the opportunity to modernize and restructure the European economy, which has seen relatively modest growth in recent years compared to China and the US.

Europe's first response to the major challenges lying ahead must therefore be to relaunch the growth process - and under the banner of environmental and social sustainability, so as not to fall into the mistakes of the past. Only in this way will it be possible to provide an effective response to the discontent of so many European citizens, as well as try to stem the new rise of populist forces that is on the horizon in Europe. In this respect, the Green Deal and the environmental transition can truly transform and revitalize the European economy, as has happened in the past thanks to other major EU transformation projects, such as the construction of the Single Market, first, and the monetary union, later (Guerrieri, 2021).

Briefly, the main features of a strategy to boost European growth through a green transition can be summarized as follows.

The transition strategy (Pisani-Ferry and Mahfouz, 2023) requires a mix of micro- and macroeconomic instruments and both public and private resources at the national and EU levels. The effort to address climate change is enormously costly. It will take a considerable amount of time to be fully implemented. It will be necessary to resist the temptation to delay implementation, as this would only increase the cost of the transition.

The sustainable growth strategy should be based on three pillars: Investment to replace energy-intensive capital (brown) with green capital (green), resources to support a new consumption and welfare paradigm, and investment in innovation to complete the transition.

Initially, public investment will drive the transition, with private investment becoming more significant in the medium to long term. In the initial phase, investment will still only serve to replace energy-intensive capital with possible negative consequences on productivity. However, incentivizing private sector involvement will require appropriate measures such as pollution taxation, subsidies for R&D and innovation and regulation.

Given the global nature of climate change, international coordination will be necessary to ensure the effectiveness of green strategies (Tyson and Zysman, 2023). As costs and benefits of climate change are unevenly distributed across countries and sectors, the temptation to behave opportunistically (free riders) may increase (this is the so-called "*tragedy of the global commons*"). The EU will thus need to define its own global strategy on climate issues (see Section 7).

However, implementing the Green Deal poses two significant challenges (Guerrieri and Padoan, 2024). First, increased productivity and benefits from the transition will only materialize in the long term, while short-term costs will be incurred. And this is because in the short-term, productivity will tend to slow down due to increased investment to replace brown capital (the so-called *"tragedy of the time horizon*")(Pisani-Ferry and Mahfouz, 2023). Additionally, the initial costs of adopting clean technologies fall disproportionately on lower- and middle-income households and businesses, exacerbating inequalities (the so-called "*tragedy of public goods*"). This suggests a time inconsistency problem for politicians and policymakers in charge of steering the transitions, where the collective benefits of the transition will only materialize in the longer run, but the costs will have to be borne by less well-off individuals in the short term. Therefore, policies aimed at increasing efficiency and productivity must be accompanied by interventions to address social cohesion and welfare throughout an early phase of the green deal. And there are already worrisome signs of a green backlash in Europe because many Member States fear the short- to medium-term economic and social costs of the Green Deal.

The scale of investment required for the energy and environmental transition is immense. Most of them will be private, but they will be preceded and accompanied by an equally large amount of public investment. Some estimates suggest well over one percent of European GDP will be needed for public investment alone (Baccianti, 2022). This figure may be conservative, considering the additional investments required for digital technologies and related services, which are integral to green and sustainable growth.

Addressing these challenges will necessitate a gigantic financial commitment from Europe and its Member States. And the calculations made so far by the Commission and other EU bodies seem to underestimate the huge common resources that will have to be found to finance the transition and intervention policies. It is a joint European commitment that will be difficult to carry out. Many European countries, including Germany, are adamantly opposed to moving in this direction. But if the current stalemate were to continue, the almost certain consequence would be that the ambitious goals Europe has set for itself in the area of climate change policy will not be achieved.

4. The key role of industry and industrial policy

The energy crisis, coupled with escalating geopolitical conflicts, has posed significant challenges to the growth model of continental European economies (Baccaro and Hadziabdic, 2023), as previously discussed, and has consequently affected their productive structures. The current hardships faced by

Germany and its manufacturing industry confirm this reality. Given Germany's status as Europe's economic powerhouse, the ripple effects of Germany's economic issues are felt throughout Europe.

A fundamental transformation of European manufacturing is imperative. It involves shifting away from energy-intensive production towards less energy-intensive industrial segments and embracing digital technologies to enhance competitiveness. This presents a formidable challenge for Europe amidst international industrial and technological competition, particularly between the United States and China, both of which are implementing expansive industrial policies and mobilizing substantial public resources.

However, achieving these goals is complicated. The objectives of a green industrial strategy extend beyond enhancing productivity and fostering innovation to encompass securing Europe's technological and industrial position. Closing the gap with the US and China in technological prowess, particularly in the digital realm, is crucial for economic security and the attainment of genuine strategic autonomy of Europe. In a geo-economic world, enhanced technological capacity serves as a deterrent and containment measure against the advancement of rival technological industries.

This is more the case as Europe's competitive lag has significant implications for key sectors central to the current digital revolution, such as microprocessors, big data, and artificial intelligence. Addressing this lag necessitates substantial adjustments and restructuring processes, which is primarily the responsibility of individual European countries. That this will not be enough and that no European country will be able to do it alone is a widespread and well-documented conviction.

Strengthening and restoring the industrial and technological competitiveness of the EU goes beyond national policies. It requires a concerted effort at the European level, avoiding protectionist tendencies and benefitting on a European scale. This is the key to success in many areas, such as AI, where Europe is particularly lagging behind. While the EU and the United States have roughly the same number of start-ups, the Americans have access to ten times more funding than their European counterparts, which allows them to scale up their industries more quickly (Figure 1).

In the digital world, we think and act on a planetary scale. To compete with non-EU big tech, Europe needs to join forces so that 'European champions' can emerge from national industrial ecosystems on a global scale. To strengthen its techno-industrial position, the EU needs to create centralized resources. This will enable the Commission to co-finance early-stage, capital-intensive critical technology projects. This applies not only to high tech, but also to defense and national security.

The first initiatives promoting economic resilience and industrial capacity, particularly in green and technology sectors, have already been made (e.g., European Chips Act, Green Deal Industrial Plan, the Net-Zero Industry Act) (Tagliapietra, Veugelers 2023). Nonetheless, the European Union is still very far from having developed an effective and adequate industrial policy strategy. For example, measures to achieve the goals in these plans of securing significant market shares for EU production concerning several green and digital technologies are lacking. Reliance solely on incentives and subsidies to alter long-term comparative advantages is relatively naïve (Aghion, 2023). On the contrary, they can easily become unaffordable.

Instead, strengthening the digital single market, increasing investment in knowledge and human capital, and enhancing venture capital funding for startups is essential. However, Europe cannot win the technology race with public money alone. It needs to unlock private capital and work hard on its overall competitiveness. Collaboration on a European scale is crucial to foster 'European champions' capable of competing globally. A focus on innovation and competitiveness is paramount, rather than striving for complete autonomy over entire production chains (Guerrieri and Padoan, 2020).

Moreover, strategic investments in critical technologies must be made, ensuring production is based in the EU and draws from a diversified supply chain. Like in quantum computing and sensing technologies. A security-driven investment plan that helps Europe's leading industrial innovators to upgrade in a collaborative way is needed for the EU's economic security posture. Important Projects of Common European Interest (IPCEIs) will be relaunched and strengthened in this respect. In the same vein, the Commission has made an interesting proposal for the creation of a "European Sovereignty Fund". Its role would be to launch EU-wide actions in clean tech frontiers where the European scale is needed. This is the case in many areas of R&D spending, where Europe has lost a lot of ground to other major competitors (see Figure 2). Yet, disagreement among Member States has hindered progress. In its place, a much less ambitious program has been approved, the so-called STEP (Strategic Technology for European Platform), initially with a budget of just 10 billion euro for the scaling-up of critical technologies, particularly in the field of digital and clean energy, but more recently with a budget of only 1.5 billion and directed entirely at defense-related projects. Such a decision is an indication of the fragile political support behind the industrial and technological agenda. Equally clear, Europe's economic security will deteriorate without a more serious promotion agenda.

Furthermore, the Commission's calculations clearly underestimate the considerable common financial resources needed to finance these industrial policies, as in the case of energy and environment. Due to the strong divisions between Member States, it will be very difficult to acquire these funds. On the one hand, there are countries like France which want to see a more assertive industrial policy. They argue that the EU needs to change course radically and adapt to the new competition among major powers. On the other hand, countries like the liberal, export-oriented open economies of northern Europe argue for substantial non-intervention under the banner of traditional free market principles. Precisely because of the divisions between Member States, the interesting proposal of the European Strategic Fund has quickly been shelved, at least for the time being.

However, with the EU lacking new common instruments and funding, its current reliance on gradual relaxation of European state aid rules in response to the US Inflation and Reduction Act (IRA) extended after Covid in March 2023 is even more worrying. The risk is distorting the single market and eroding cohesion among Member States. Indeed, the strongest countries, first of all Germany, will take advantage of this, as it happened during the recent energy crisis, triggering a subsidy race and creating new deep divergences between member countries. Though difficult, a common policy agenda is necessary to enhance Europe's industrial and technological capability and safeguard its economic security (Guerrieri and Padoan, 2024).

5. Deepening the Single Market and reconfiguring GVCs

One of the most significant risks confronting Europe today is the potential further relaxation of European state aid rules, which could compromise the integrity of the EU's internal market. The Single Market not only stands as a cornerstone of European competitiveness but is poised to become the focal point for the EU's sustainable growth with the Green Deal, once the current over-reliance on exports is diminished. However, its effectiveness needs to be reinforced and complemented with policies and measures aimed at safeguarding its vital interests, thus becoming a cornerstone for building the EU's strategic autonomy in terms of heightened competitiveness and security.

Firstly, a new and effective EU green industrial policy should aim at enhancing the overall attractiveness of the EU's internal market as a green investment destination. This entails completing the Internal Market (IM) by encompassing service sectors that have remained outside its purview, notably in energy, telecommunications, and digital diffusion (Fig. 3). Services account for a significant share of GDP in all advanced economies and are poised to shape the future global economy. Even the growth gap between the European Union and the United States counts among its main causes Europe's lower productivity growth in those service sectors in which the integration process is most deficient (Guerrieri and Padoan, 2020).

Manufacturing services - the so-called advanced tertiary sector - have become a fundamental and complementary input for the industry. They include digital services, and in particular knowledge-intensive business services (KIBS), where the EU's competitiveness has declined significantly in recent years. These are all fast-growing sectors that are driving structural changes and productivity gains essential for countries' long-term economic growth in the ecological and digital transition.

The deeper integration of the services market could thus be pivotal for Europe's future competitiveness. Further liberalization and integration within the internal services market could provide strong incentives for the restructuring of European economies and enterprises at a continental scale, fostering positive changes in production and innovation systems, leveraging economies of scale, and facilitating appropriate facility relocations within the EU. A recent IMF study suggests that deeper integration within the EU could potentially boost Europe's GDP by 7 percent (IMF, 2023).

Moreover, the internal market could serve as a robust foundation for the reorganization or establishment of European value chains in the face of new strategic and security conditions. It is important to recall that the EU is highly integrated in GVCs in both manufacturing and services, with considerable heterogeneity across EU Member States in terms of the degree of dependence on GVCs. Deep and resilient value chains are therefore crucial for Europe's economic competitiveness in the long term (Bontadini, et al., 2023).

GVC disruptions caused by the Covid pandemic and the war in Ukraine have led not to re-shoring, as many had expected, but to greater diversification (and nearshoring), along with a shift from global to regional supply networks. To address these challenges, the EU should leverage new international partnerships and trade relations, accompanied by financial support, to promote the diversification of critical value chains (see Section 7), thereby strengthening them and mitigating risks of economic dependency, including potential export restrictions on critical commodities.

Despite certain weaknesses that make Europe particularly exposed to the changes taking place globally, the EU's diverse composition of advanced and emerging economies positions it favorably to restructure its production offer in terms of value chains (Guerrieri and Padoan, 2024)). Its mix of innovation and manufacturing strength presents a unique ecosystem compared to the US, which is relatively more specialized in innovation, and China, which is more focused on manufacturing, enabling it to respond more effectively to the pressures of economic fragmentation. Ultimately, the EU has the potential to reorient global production towards low-cost, low-adjustment production sites in Eastern Europe, thereby enhancing its economic resilience and security.

6. Protecting European strategic interests and the over-dependence on China

The green transition is highly mineral-intensive and will significantly increase the EU's demand for specific critical materials essential for the environmental and digital transformation. Currently, most of these materials are sourced from outside the EU, primarily from China (Fig. 4). In fact, the EU imports 93% of its annual consumption of strategic materials from China, rendering it vulnerable to external shocks and potential trade weaponization. To mitigate this risk, the EU must ensure secure and reliable access to critical materials.

To address this challenge, alongside the industrial policies mentioned earlier, the EU initiated the European Raw Materials Alliance (ERMA) program in 2020 (European Commission, 2020). The ERMA aims to enhance the EU's autonomy in critical material supply for the energy and digital transition. Additionally, in March 2023, the Commission introduced the Critical Raw Materials Act, a comprehensive set of measures to achieve a "secure, diversified, and sustainable" supply of strategic raw materials. These measures include diversifying supply chains, increasing domestic production, and promoting recycling and recovery of critical materials, thereby strengthening the circular economy (EuropeanCommission, 2023).

However, safeguarding against asymmetric interdependencies that may jeopardize EU security extends beyond addressing over-reliance on strategic materials. In line with the European Economic Security Strategy launched in June 2023, as mentioned at the beginning of this paper, the European

Commission recently proposed various measures. Among the many proposals and initiatives, those in favor of a revision of the European law on the control of foreign direct investment are worth mentioning (European Commission, 2024). Under these measures, all Member States would be obligated to introduce FDI monitoring and impose bans on investments that pose threats to European security. This contrasts with the current scenario, where not every country has FDI laws, and the criteria for their application vary widely. Furthermore, the scope of control would extend to investments from within the EU if the investors are controlled by foreign companies. However, the potential damage stemming from the implementation of restrictive measures must be carefully considered when calculating security risks, and discretion in using such instruments should be carefully monitored to prevent protectionist abuse by Member States.

Regarding outbound investment control, an even more controversial issue, the Commission has published a White Paper, which intends to launch a debate and discussion among Member States with a view to drawing some policy conclusions. The White Paper is also devoted to the issue of more effective EU controls on the export of dual-use goods (civilian and military), which may pose security problems within the EU. Calls for a coordinated EU-wide approach in such cases have intensified following pressures last year from the US on the Netherlands to impose restrictions on the Dutch chip equipment supplier ASML.

While the Commission advocates for "Europeanization" of EU security rules to ensure consistency among Member States' measures, the latest proposals are not in the direction of interventions at the EU level. Primarily they urge Member States to take further action and engage in consultations for additional policy initiatives. It should also be considered that the evolving global landscape necessitates adaptive responses to shocks, including the use of "offensive" instruments like sanctions alongside defensive ones. But this is a difficult area for Europe to enter. The EU's treaties, designed to uphold openness to international investment and finance, prohibit restrictions on capital and payment movements between the EU and third countries. Consequently, strengthening the EU's ability to act effectively on the international stage is essential.

All these instruments were initially crafted with an implicit focus on China (Beaucillon, 2023), although they were designed to be applicable in a broader context concerning dealings with third countries. Indeed, particularly in strategic sectors like clean energy, where items such as batteries for electric vehicles, photovoltaic panels, wind turbines, and critical materials are vital, Europe's primary concern is mitigating its over-reliance on Chinese companies and global supply chains. This is accentuated by China's reputation as an unfair competitor, characterized by massive subsidies to its companies and a disregard for workers' rights. Establishing reciprocity and a level playing field in economic relations with Beijing is thus imperative.

Relations between Brussels and Beijing have further soured as China emerges as an assertive systemic rival on the international stage. More recently, China's stance of "active neutrality" regarding Ukraine, often perceived as veiled support for Moscow, and its unequivocal statements regarding reunification with Taiwan, exemplify the escalating tensions.

More recently, the EU has proposed a strategy of "de-risking" to address vulnerabilities stemming from economic interdependence while preserving an open global economy. In the case of China, this strategy aims to prioritize national and European security interests in economic and political dealings with Beijing (Guerrieri and Padoan, 2024). Unlike the American proposal of "decoupling" from China, which is deemed unfeasible due to huge and intricate production and trade ties between the two superpowers, Europe favors a strategy focused on managing risks rather than abrupt disengagement. It is worth noting that the United States has also recently embraced the idea of "de-risking", although specific details regarding the strategy's implementation remain elusive (Sullivan, 2023). However, close collaboration with the US administration empowers Europe to exert greater influence over Beijing.

Nevertheless, the EU's internal disunity remains a significant obstacle in its relationship with China. Individual Member States' interests often take precedence, hindering the implementation of a unified and effective strategy of confrontation and competition with Beijing. While some Member States have taken steps to enhance economic security by adopting measures against China, different views on China persist within the EU. This lack of cohesion allows China to exploit divisions within Europe, undermining its ability to negotiate independently on the international stage (Bergsten, 2022). Achieving consistency and unitary European strategy should thus be a paramount objective of a unified European economic security strategy.

7. Open strategic autonomy and the presence of the EU in the world

Europe is the world's largest trader and recipient of foreign direct investment (Fig.5). Openness and international cooperation will remain essential for Europe. Consequently, strategic autonomy cannot mean that the EU becomes more closed to the world. On the contrary, by reducing its excessive external dependence and strengthening its technological power, Europe must do all it can to protect and reform the international economic order and prevent the world from fragmenting.

A divided world into two blocs or disorderly economic fragmentation would severely harm and marginalize European economies (Georgieva et al., 2022). Therefore, Europe must advocate an open world economy while considering new geopolitical and security dynamics.

Trade policy is a crucial tool for bolstering Europe's international presence, but it must align with Europe's strategic interests and adapt to the evolving global context (Hoekman and Puccio, 2019).

The current global trade regime is marked by rising protectionism, economic policies used for geopolitical ends, and the waning influence of the WTO (Dadush, 2022). In response, Europe's strategy should not only adhere to multilateral WTO rules but also consolidate its network of bilateral agreements worldwide. These agreements should not solely focus on trade but also on economic security and expanding Europe's strategic relations, especially with countries rich in critical materials.

Europe's trade strategy should extend beyond traditional partners and engage with emerging powers in the Global South, such as India, Turkey, Brazil, and Saudi Arabia. Strengthening alliances with like-minded countries is crucial, but Europe must also diversify its relations with other third countries, particularly those in the Global South, even if they are not aligned with European values and alliances. India and Brazil come to mind immediately. They are potential and highly relevant partners for diversifying Europe's relations with exponents of the developing world.

Similar to China's New Silk Road initiative, Europe must enhance its engagement with Africa, a continent of strategic importance. However, the involvement of authoritarian regimes such as the ones in Beijing and Moscow in many African countries must lead Europe and other Western countries to rethink their approach to the continent. Europe should differentiate its approach by upholding transparency and openness standards in its investments. Moreover, defining an effective new policy to support the export of raw materials, especially strategic raw materials, from these less developed countries to Europe is insufficient. The creation of local industries will have to be promoted, with agreements that could have positive spin-offs and mutual benefits, for example in terms of migration management policies.

This renewed engagement with Africa and other developing regions requires substantial investment, contrasting with recent underinvestment. Otherwise Europe risks returning to the empty declarations and conferences of the recent past, which were not followed by action. Europe must revamp instruments and mechanisms such as Association Agreements, aid and development cooperation tools. The EU is the largest donor of development aid in the world. But it distributes it in a fragmented way. There is no real coherent strategy. One important instrument could be the so-called Global Gateway Initiative. It has a budget of 300 billion euros. It holds promise but must be operationalized and implemented more effectively than previous initiatives.

Indeed, reforming the international economic order is crucial, and Europe can play a pivotal role in this endeavor by engaging with countries from the Global South. A pragmatic approach to multilateralism is essential to tackle pressing global challenges, including economic security concerns like regulating artificial intelligence, cybersecurity, and environmental sustainability. These are global public goods that can only be provided by means of international cooperation agreements (IMF, 2022).

In this perspective, the reform and strengthening of multilateral institutions responsible for the design and enforcement of international rules is the best way to ensure Europe's security and economic growth. Europe should take the lead in reforming multilateral institutions like the World Trade Organization (WTO) to adapt them to the complexities of a multipolar world. It should also be emphasized that the opening of trade can no longer be pursued in isolation from other areas of global governance, such as the environment, health, financial stability, respect for human rights and, above all, social issues. In the past, the WTO was at least partly linked to other international organizations such as the IMF and the World Bank. This remains important. But it is no longer sufficient. To deal with the new trade-offs and to ensure necessary compatibility between different agenda items, such as trade and environment or trade and security, linkages between negotiating areas need to be strengthened and broadened. This is also the case regarding the positive effects of issue linkage on countries' cooperation.

Finally, one should not overlook or underestimate the growing skepticism and resistance towards trade agreements in advanced economies, including Europe. So much so that some of them, including important ones (CETA, Mercosur), have not yet been ratified or are only provisionally applied. Workers and citizens are in favor of an open economic system, but they also want it to protect them. There is a need for the strengthening of social and welfare policies to mitigate the unequal impact of free trade within societies ("open and inclusive strategic autonomy"). Both national governments and the EU have a significant role to play in this regard; certainly, much greater than the one played so far.

In conclusion, the EU needs to do more to prevent the decline of multilateral governance at a global level. If Western countries, along with leading Southern countries, do not take the initiative to reform and modernize the global order, there is a risk of leaving the field open to countries that view regional formats like BRICS as a means of rupturing the existing global order rather than fostering dialogue. To exert influence globally and enhance its open strategic autonomy and economic security, however, Europe must become a stronger and more assertive actor both politically and economically on the international stage.

8. European public goods and EU governance

The European Union is facing a monumental task: establishing an autonomous capacity to assert and safeguard its economic-strategic interests, encapsulated in the concept of open strategic autonomy. It is a matter of strengthening Europe's competitiveness while enhancing its economic security.

However, charting this path forward is no easy feat. It requires addressing a myriad of complex domestic and international trade-offs and challenges. And it will not be easy, as we have seen, to identify the problems that need to be addressed, together with the policies and the instruments of intervention that need to be used.

Mere reinstatement of past policies won't suffice to deal with the major challenges, from the ecological transition to industrial and technological competition, to revitalizing relations with the Global South countries. Europe must adapt and innovate to meet these new tests head-on. Some steps have already been taken, and they are in the right direction, but a great deal remains to be done.

Central to Europe's agenda for greater competitiveness and strategic autonomy is the provision of so-called European Public Goods (EPGs) (Buti et al. 2023), spanning climate policy, energy security, and industrial and technological endeavors. In all of them, the Union represents an essential means for individual European countries to recover their sovereignty and capacity for action in areas and fields where individual efforts fall short (Draghi 2019).

Nevertheless, realizing these EPGs necessitates additional political instruments and financial resources at the European level. Only through a profound restructuring and renewal of its economic governance architecture can Europe equip itself (Guerrieri and Padoan, 2023).

The current decision-making mechanisms are labyrinthine and cumbersome, ill-suited for agile crisis management. Overcoming the unanimity rule in favor of qualified majority voting in pertinent fields is imperative to facilitate swifter, more effective decision-making aligned with Europe's growth and security objectives.

Furthermore, there is an urgent need for augmented common financial resources. The ecological and digital transition requires a monumental investment, spanning both public and private sectors. However, individual Member States, already burdened by public debt consolidation, cannot shoulder the full financial load. Moreover, the new Stability and Growth Pact, enacted in 2024, leaves limited fiscal space for Member States to address the additional financial demands associated with the green transition.

It requires the creation of an investment and financing capacity at European level. For instance, joint financing and investment programs to initiate energy transition policies and develop an autonomous European technological capability. They should be financed by the issuance of EU sovereign debt and should be centrally managed. However, unlike the NGEU, joint investments should be neither limited nor temporary; they should be made permanent.

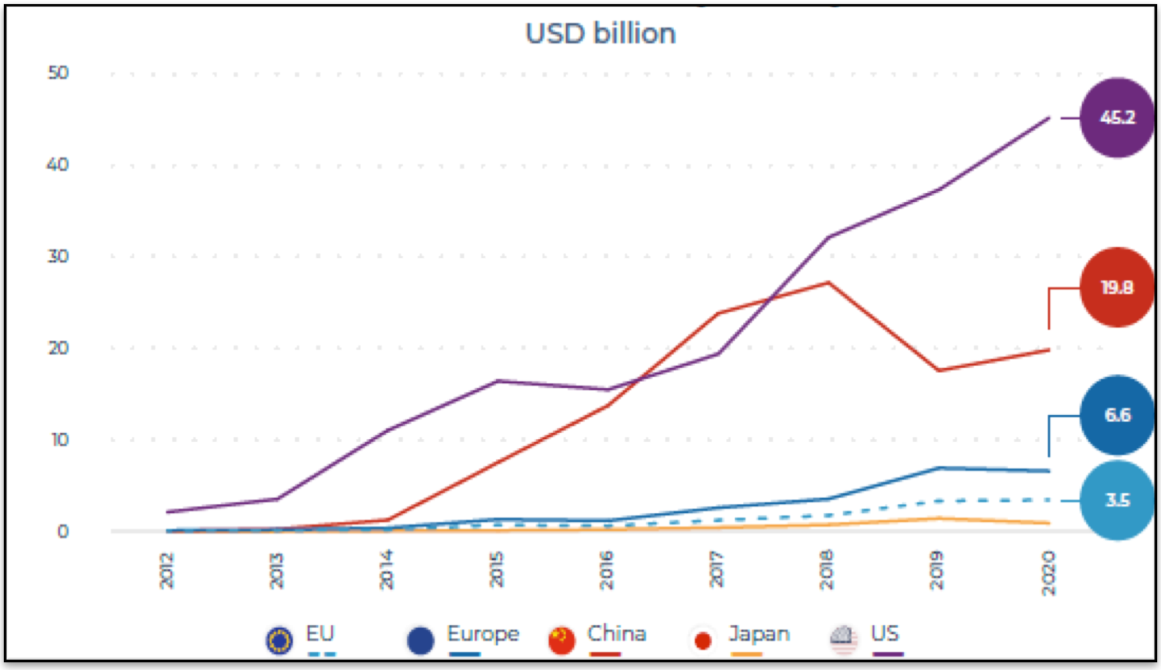
Increasing the allocation of "own resources" to European institutions and granting them new fiscal powers could serve as another important solution to address the challenges ahead. This step would mark the beginning of a common fiscal capacity at the European level, crucial for financing the substantial public expenditure required for Europe's environmental transformation. A centrally managed fiscal capacity of significant size would also ensure that resources be allocated based on where they can generate the greatest benefits, rather than being dependent on individual countries' capacity and willingness to provide state aid.

Furthermore, budget reforms are essential to finance the ambitious policies the Union will pursue in the coming years. The success of programs like Next Generation EU (NGEU) by 2026 would be crucial to demonstrate the advantages of common financing and centrally managed fiscal capabilities for all Member States.

Addressing the scarcity of resources for private investment across Europe is another critical aspect. Currently, this scarcity persists partly due to the underdeveloped state of the Unification of the European capital markets, hindered by the incomplete European banking union and the absence of a European safe asset. Completing both the Banking Union and the Capital Markets Union is thus imperative. Without fundamental steps in this direction, achieving the dual green and digital transition in Europe would remain elusive.

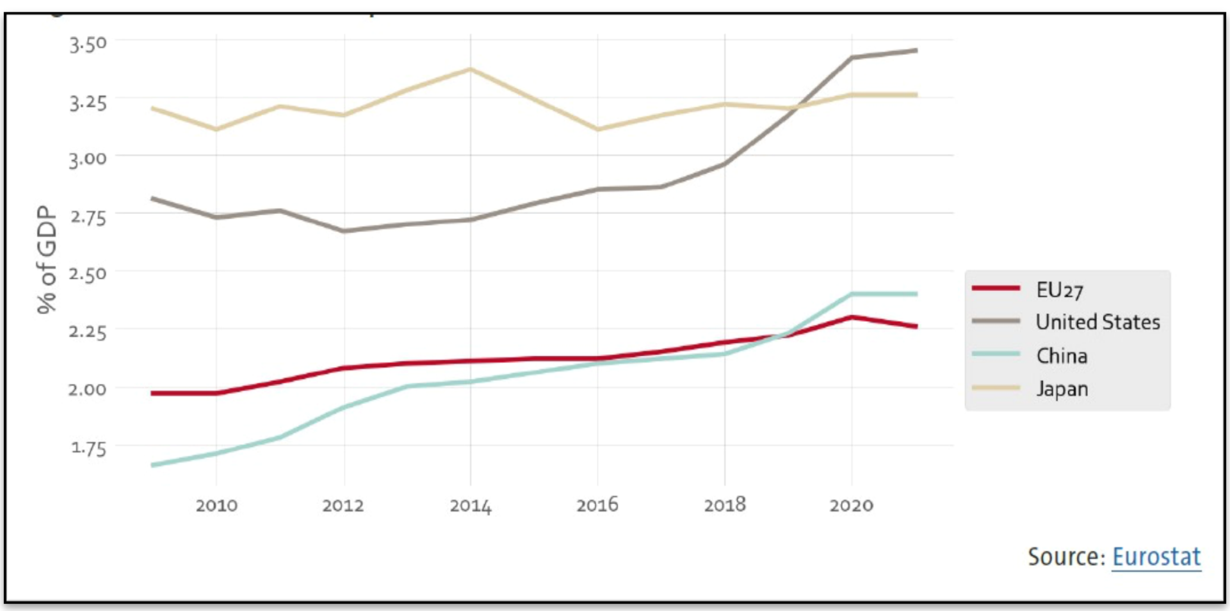
Regrettably, little to no progress has been made in these areas in the recent period. If anything, there have been a few steps backwards in the last two years. However, Europe must undergo a profound restructuring and revitalization of its economic governance architecture to equip itself for the challenges ahead. This entails surmounting bureaucratic hurdles, enhancing decision-making agility, and securing the required financial resources. Maintaining the status quo risks rendering European countries irrelevant and marginalized in a fragmented and conflict-ridden world. What is urgently needed is a significant strengthening of the Union's sovereignty and resilience to advance open strategic autonomy while safeguarding economic security and competitiveness. The key challenge for the future global growth of the Union lies in taking decisive steps in this direction by setting up a policy response that suits the new geopolitical environment. One question that arises is the sustainability of the arrangements, keeping in mind that the EU must at the same time establish an equilibrium between Member States and an equilibrium vis a vis the other global key players. In both cases the EU must rely on a strong identity. Certainly, a strong sovereign Europe would be a necessary condition for reaching such a target (Guerrieri and Padoan, 2024).

Fig. 1 Venture capital investment in Artificial Intelligence by country



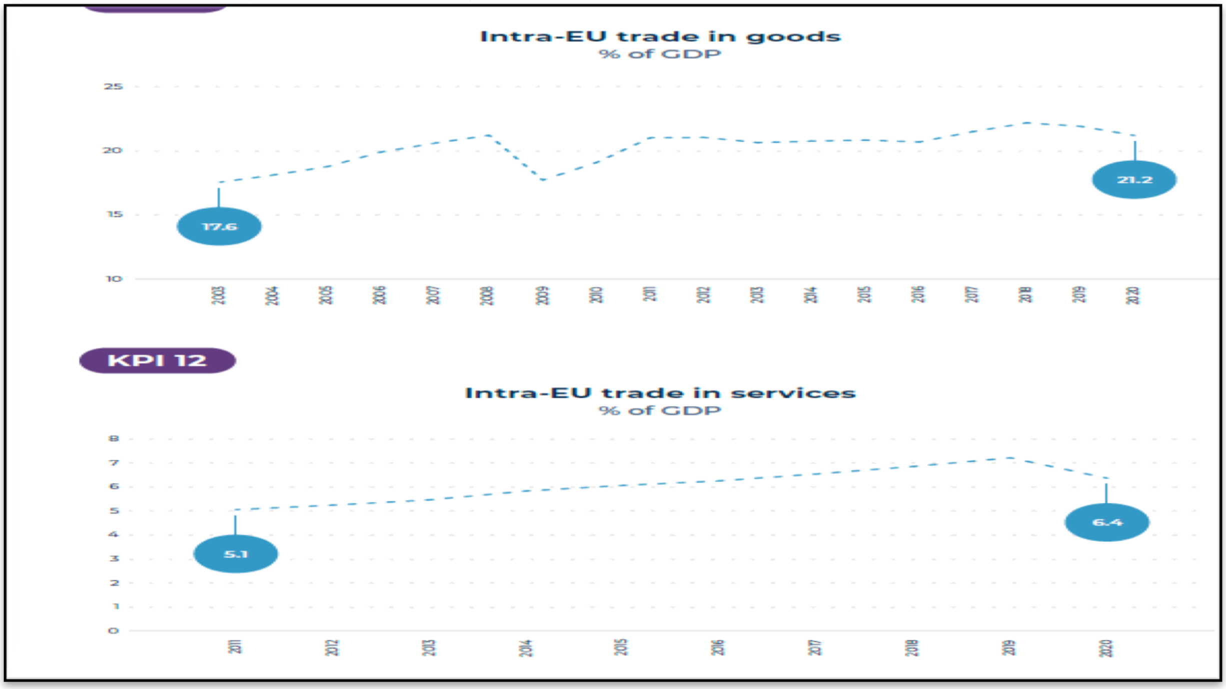
Source: ERT, European Competitiveness & Industry, Benchmarking Report 2022

Fig. 2 Domestic Expenditure in R&D in terms of GDP



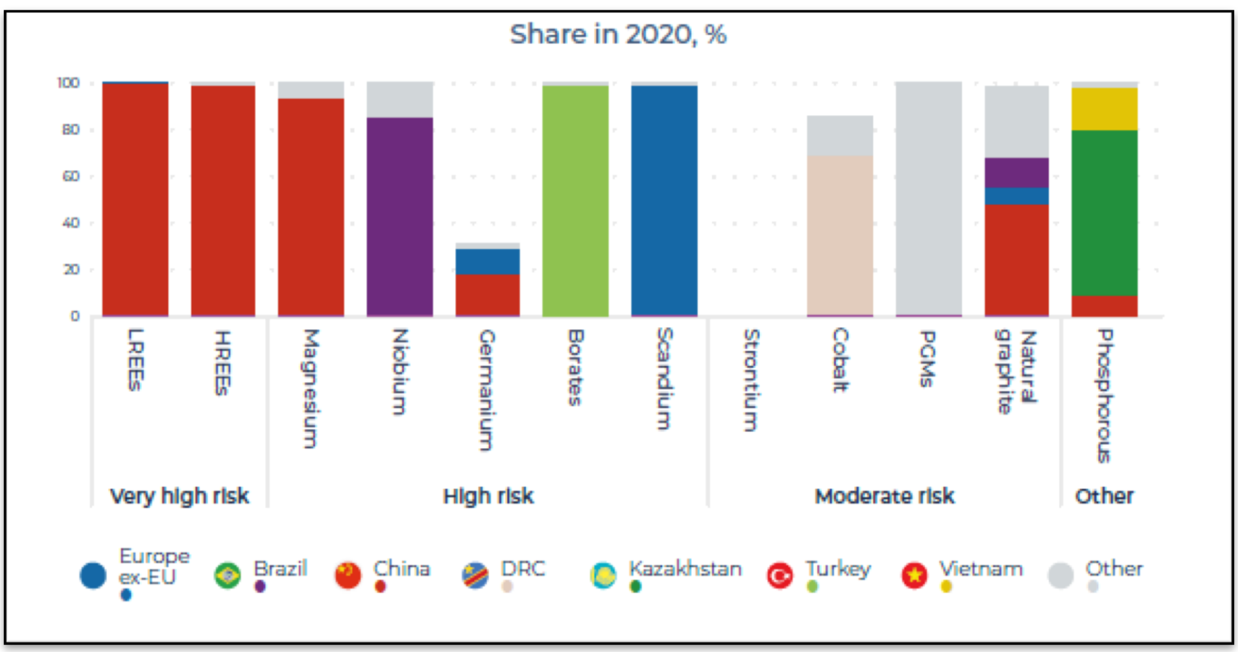
Source: EUROSTAT

Fig. 3 The EU Single Market for goods and services



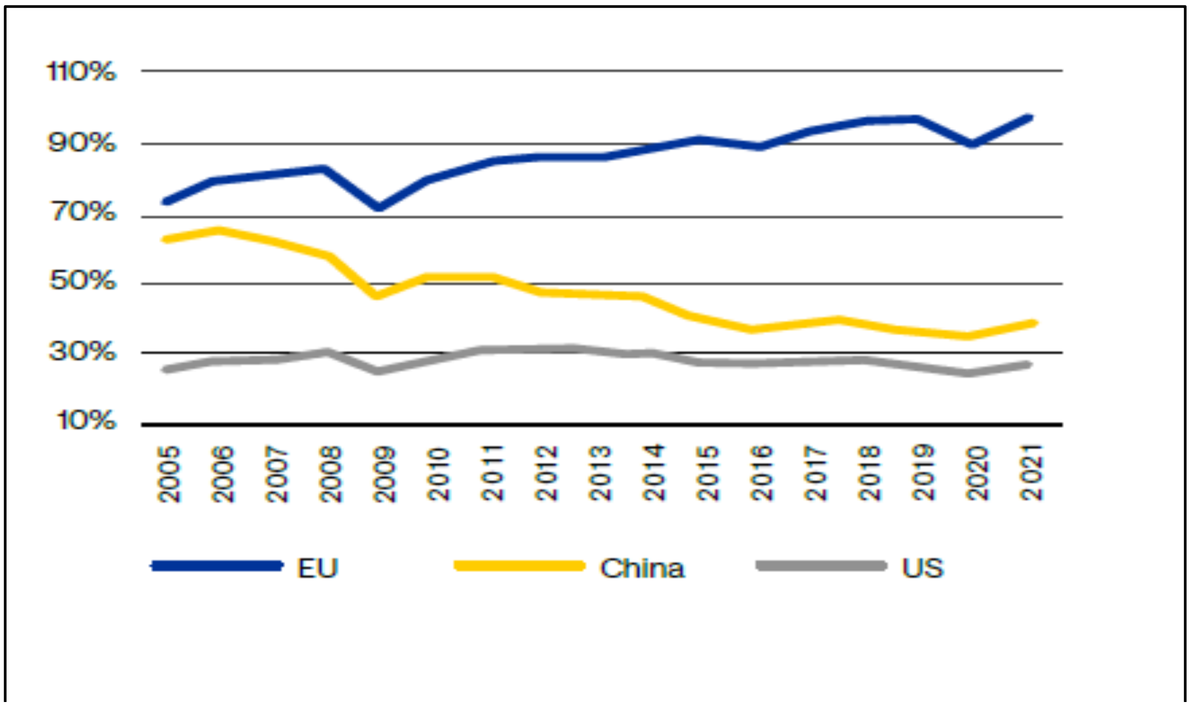
Source: ERT, European Competitiveness & Industry, Benchmarking Report 2022

Fig. 4 EU Import reliance on critical raw materials and main sourcing countries



Source: ERT, European Competitiveness & Industry, Benchmarking Report 2022

Fig. 5 TRADE OPENNESS OF EU, CHINA, US (Export + Import /GDP)



Source: IMF, Data Set

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