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LUHNIP Monthly brief on EU Industrial Policy

March 2024

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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.

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Last Month in Brief

- **4 March:** European ministers for Environment and Energy meet in Brussels for the Transport, Telecommunications and Energy Council to discuss energy prices and supply, as well as the state of the solar power industry in Europe.
- **5 March:** The European Commission and the High-Representative for External Affairs present the *Defence Industrial Strategy* (EDIS) and the *European Defence Industry Programme* (EDIP) (**see Deep Dive 1**).
- **6 March:** The Council of the European Union and the European Parliament reach an agreement over the EU Cyber Solidarity Act aiming at strengthening EU cyber security capacities.
- **7 March:** European ministers for Economy and Industry meet in Brussels for a Competitiveness Council to discuss measures to strengthen the competitiveness of European industry.
- **11-14 March:** The European Parliament meets in plenary to adopt, among other texts, the Artificial Intelligence (AI) Act and the Forced Labour Regulation.
- **15 March:** The COREPER approves the Corporate Sustainability Due Diligence Directive.
- **18 March**: The Council adopts the Critical Raw Materials Act (**see Deep Dive 2**).
- **20 March:** The European Commission adopts the communication on *Building the future with nature* which proposes actions to boost biotechnology and biomanufacturing in the EU, as well as its action plan to address labour and skills shortage in the EU.
- **23 March**: European Heads of State and Government meet in Brussels for a European Council devoted, among other topics, to the enhancement of EU strategic autonomy.
- **25 March:** The European Commission opens five non-compliance investigations into Alphabet, Apple and Meta's practices in the framework of the Digital Markets Act (DMA) (**see Deep Dive 3**).

[1] We thank Stefano Chiappo, Romain Cohen, Giulio Petrillo, and Francesco Rosazza Boneitin for their excellent research assistance.

Deep Dive 1: The presentation of the EDIS and EDIP by the European Commission and the EEAS

The first-ever "European Defence Industrial Strategy" (EDIS) was presented on 5 March 2024 by Commissioners Thierry Breton and Margrethe Vestager and High Representative of the Union for Foreign Affairs and Security Policy Josep Borrell. The publication of the Strategy was accompanied by that of the "European Defence Industry Programme" (EDIP), the operational plan for its implementation. Alongside the 2022 Strategic Compass for Security and Defence, they define the EU's long-term strategy in the sector. In a geopolitical context marked by the war in Ukraine, the worldwide increase in national defence capabilities and the US' possible disengagement from Europe in 2025, the EDIS sets out 3 clear objectives:

1. *to increase the production capacity of the European defence industry;*
2. *to strengthen European cooperation in the sector;*
3. *to reduce dependence on third countries (notably on the US).*

To achieve these objectives, the EDIS proposes to improve existing instruments (e.g. by including Ukrainian companies in these initiatives), but also new ones such as:

- the *Structure for European Armament Programme* (SEAP), which aims to foster defence cooperation between Member States by providing increased funding and simplified/harmonised procurement procedures. Member States will also benefit from VAT exemptions when they are joint owners of equipment purchased through SEAP.
- the *European Military Sales Mechanism* (EMSM), which aims at facilitating the availability of defence products from the EU's Defence Technological and Industrial Base (EDTIB) by providing financial support for the pooling of readily available defence capabilities, and provisions to ease procurement processes and capacity building measures for procurement agents.

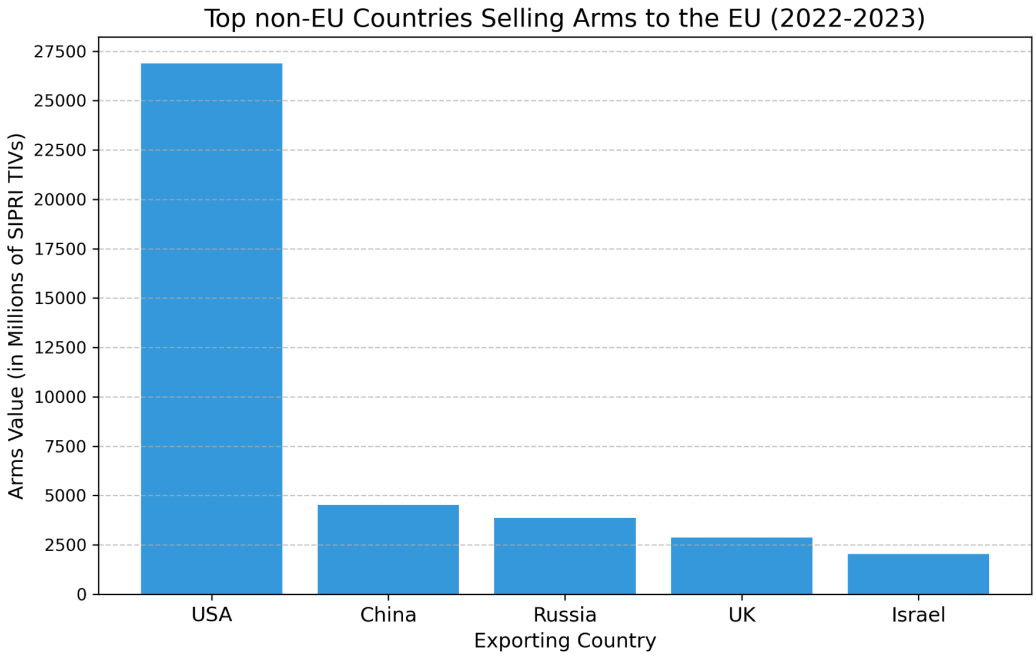
The EDIP is a budgetary and regulatory instrument for EDIS' implementation. It provides €1,5 million from the EU budget to support the existing *Act in Support of Ammunition Production* (ASAP) and the *European defence industry reinforcement through common procurement Act* (EDIRPA). It will also contribute to support the *Fund to Accelerate defence Supply-chains Transformation* (FAST), a new fund designed to facilitate access to debt and/or equity financing for SME's. EDIP also envisages the creation of a *Defence Industrial Readiness Board* (DIRB) to oversee the EU's joint programming and procurement missions and monitor EDIP's implementation. Finally, through EDIP, the European Commission will launch "European defence projects of common interest" linked to the priorities identified in the framework of the existing Coordinated Annual Review on Defence (CARD) and the Permanent Structured Cooperation (PESCO) processes.

LUHNIP's take

The presentation of the European Defence Industrial Strategy (EDIS) and the European Defence Industry Programme (EDIP) by the European Commission shows a clear willingness to increase the output of the European defence and technological base (EDTIB) in a challenging geopolitical context and after years of downsizing. However, despite the ambitious targets set, the instruments proposed in the communications remain intergovernmental in nature, with defence policy remaining largely the competence of Member States. This

method has limits - as shown by the first assessments of the Permanent Structured Cooperation (PESCO) mechanism but also by the limited use of new EU investment tools to encourage the acquisition of weapons from third countries. At the same time, it has not stopped the European industry to favour technological partnerships with extra-EU partners. It is therefore doubtful whether the continuation of the intergovernmental method without strong political incentives will enable the EU to reinforce the EDTIB and reduce its dependence on the United States for the supply of weapons (as shown in Figure 1).

Figure 1: Arms imports into the EU by third country of origin



Source: SIPRI Database.

Doubts emerge also concerning the long-term financing of the European defence industrial strategy. The €100 billion fund proposed by Commissioner Thierry Breton in January 2024 was not mentioned in the final communication by the European Commission on EDIP. The programme only includes an additional budget of € 1.5 million for the period 2025-2027, which is identical to that allocated to the European Defence Fund (EDF) at the European Council in December 2023 (see our December 2023 Monthly brief). There is thus a strong discrepancy between the European Commission and the European External Action Service's political ambitions and the proposed instruments to achieve them. More political, budgetary, institutional efforts will be needed to allow for the emergence of a genuine European defence industry to meet today's geopolitical challenges.

Deep Dive 2: The adoption by the Council of the Critical Raw Materials Act on 18 March

On 18 March 2024, the Council of the European Union issued its final approval for the *Critical Raw Materials Act* (CRMA), making it the last step in the legislative decision-making process before its application. The main elements remain identical to the November 2023 Council-EP agreement on the issue (see our November 2023 Monthly Brief), which:

- identifies two lists of materials, 34 critical and 17 strategic, labelled as key for the green and digital transitions, as well as for the defence and space industries;

- sets ambitious 2030 objectives for the consumption of raw materials to reduce the dependence on third countries:
    - at least 10% from EU extraction;
    - at least 40% from EU processing;
    - at least 25% from domestic recycling;
    - not more than 65% of each strategic raw material at any relevant stage of processing from a single third country.

- expedites permitting procedures by foreseeing a maximum period of 27 months for extraction projects and a 15-month one for recycling products.

- calls for companies manufacturing strategic technologies to conduct risk assessment procedures and develop mitigation strategies to prevent and properly face eventual supply-chain disruptions.

Regarding trade policy, the diversification of the EU's supply in critical raw materials is promoted by means of new agreements with countries rich in rare-earth elements. In particular, the Act calls for expanding the network of *Sustainable Investment Facilitation and Free Trade Agreements*, but also setting up a *Critical Raw Materials Club* open to countries interested in strengthening global supply chains.

LUHNIP's take

The final adoption of the Critical Raw Materials Act by the Council is a significant event – alongside the adoption of the Net Zero Industry Act in February 2024 (see our February 2024 Monthly Brief). These are two major pieces of legislation in the European Commission's Green Deal Industrial Plan. The guidelines adopted by the EU institutions constitute a notable response to strengthen the EU's strategic autonomy in the supply of critical raw materials for the dual transition by means of: the setting of important benchmarks for raw materials' consumption, the acceleration of permitting procedures for extraction and recycling projects, but also the promotion of an active trade policy to reduce the EU's dependence on a small number of third countries (a list of the recent efforts in the EU's Raw Materials Diplomacy is available here. The legislation also responds to the recent demands of the European industry for an acceleration of permitting procedures for investment projects and a secure access to critical raw materials.

However, to catch up effectively with its competitors in this area – notably China – and to respond to the growing demand for these materials – e.g. for batteries – setting ambitious targets will not be enough. Additional incentives for European companies will be needed to extract the critical materials available on European soil. Moreover, the challenge is for the new European diplomacy on critical materials to strike the right balance between industrial and environmental objectives and respect for human rights.

Deep Dive 3: The opening of non-compliance investigations into Apple, Google and Meta's practices in the framework of the Digital Markets Act

On 25 March, the European Union opened five investigations into Alphabet, Apple and Meta's practices for non-compliance under the Digital Markets Act (DMA). On 6 September 2023, The DMA designated six gatekeepers – Alphabet, Amazon, Apple, ByteDance, Meta, Microsoft - required to comply with a list of 22 positive and negative obligations by 7 March. After reception the companies' reports on the status of their implementation, the European Commission decided to launch investigations into Alphabet, Apple and Meta's practices to verify the compliance of these companies' practices with the DMA rules.

Alphabet and Apple are suspected of multiple prohibited behaviours: first, anti-steering practices, regulated under Article 5(4) of the DMA. Previously, Apple received a fine amounting to €1,8 billion following its decision to prevent the Swedish company Spotify from communicating payment options to its users outside of the Apple Store in 2020. The tech giant claims to allow third-party app stores on iOS devices but imposes a yearly fee per user for larger apps and restricts collaboration with those switching app stores, potentially maintaining unfair dominance. Additionally, according to the European Commission, Apple's web browser Safari layout design may limit users' choice, violating Article 6(3) of the DMA. When it comes to Alphabet, concerns have been raised over potential self-preferencing. Alphabet's search engine would favour its services, such as Google Shopping and Google Flights, at the expense of other services.

Finally, the Commission is leading an inquiry against Meta for its recent pay or consent model, which offers the consumer a binary choice: i.e. to accept the processing of personal data for commercial purposes or to pay to access the application. According to the European Commission, this choice does not provide alternatives to consumers nor prevents the accumulation of data by gatekeepers – which is prohibited under Article 5(2) of the DMA.

LUHNIP's take

Since the mid-2010s, the European Commission has been imposing fines against US tech giants in breach of EU antitrust rules. This includes a €2.42 billion fine on Google in 2017 and a recent 1.8 billion fine on Apple concerning access to its music streaming services. Launching investigations against Apple, Google and Meta within the framework of the Digital Markets Act is a significant further step in the European Union's strategy to regulate the power of US big tech companies.

If found non-compliant with the DMA rules, these companies risk being fined up to 10% of their total annual turnover, possibly up to 20 % in case of repeated violations. Such fines may have important consequences on the activities of these companies. Finally, the fact that the EU intends to conclude the proceedings within a year – thus much faster than previous multi-year antitrust investigations against US tech giants – signals the Commission's willingness to seriously step up its actions.

Such interventionism by the Commission is taking place in a global regulatory context increasingly targeting these companies' operations. For example, in July 2023, the Australian government proposed a

"Communications Legislation Amendment bill" to combat disinformation on social media, giving powers to the Australian Communications and Media Authority (ACMA) to impose fines worth up to 5% of their annual global turnover. During the last years, the United States' Justice Department filed several cases against Google and Meta for breaches of US antitrust rules. It also recently sued Apple with charges of monopolising the smartphone market. The outcomes of these trials will have important consequences on the functioning of the US big tech companies and on their future cooperation.

Guest Contribution of the Month

Simone Vannuccini, *Université Côte d'Azur and GREDEG, CNRS*
Olimpia Fontana, *Centro Studi sul Federalismo*

European industrial policy for strategic autonomy and green transition

When Albert Hirschman wrote *National Power and the Structure of Foreign Trade*, the link between nationalism-inspired trade policies and conflict became crystal clear. Nowadays, we experience a comparable situation as we enter a new phase in globalisation. This is characterised by growing rivalries emerging in response to compounding crises of planetary scope – the so-called poly- and permacrisis. Countries increasingly favour state intervention in the economy to reduce their vulnerabilities; in practice, this means that industrial policy is returning to the spotlight.

Industrial policy inspired by open rivalries might result in economic growth but has a fundamental downside: it undermines international cooperation and feeds claims of sovereignty and inward-looking nationalistic attitudes. Recent initiatives such as the Inflation Reduction Act (IRA) in the US illustrate the double-edged nature of modern industrial policy: on the one hand, public investments (especially in critical and green technologies) are now widely accepted in virtue of their positive externalities; on the other, local content requirements are in plain clash with WTO principles. Similarly, trade policy becomes weaponised to avoid "technology leakage" of strategic assets (think of semiconductors export bans towards China).

We claim that, in Europe, the negative spillovers produced by competitive industrial policies might be overcome by building a federal industrial policy of the European Union (EU), centred on the themes of strategic autonomy and the green transition. Many proposals along these lines exist (including Ursula von der Leyen's idea, launched in 2022 and later downsized, to create a European Sovereignty Fund (ESF). However, the question of how such an overarching programme can be institutionalised still stands. The key headwinds to European industrial policy are political – as intervention in the domain of industry is a matter of State intervention, and the EU is not a federal State yet. However, current external pressures create not only risks, but also an unbalanced situation from which new power arrangements can emerge. We have witnessed a glimpse of that with the institutional innovations launched in reactions to the Covid-19 pandemic under the Next Generation EU (NGEU) package; however, its radical novelty was constrained by the temporary nature of the initiative. The true challenge is to make institutional innovations in this domain permanent.

Our proposal is to establish a broad institutional platform, that is, a framework fund for a European industrial policy, building on the NGEU model and the ESF idea. The fund can be established as a non-permanent vehicle, but with a longer timeframe, and financed through the proceeds of EU bonds. The rationale for its establishment

could be based on the emergency provisions of Art. 122 TFEU, possibly resorting to consensus on the emergency unfolding in the context of the permacrisis, and on the principle of fairness in the distribution of support across Europe. We suggest an architecture based on a two-tier structure. The first tier is represented by the existing Important Projects of Common European Interest (IPCEI) instrument, currently providing "European public goods by aggregation" (with national delivery and European financing). We advocate for the Europeanisation of IPCEIs, evolving into European pure public goods (with both European delivery and financing). A second level will be based on centrally managed programmes, designed to overcome the shortcomings of the existing InvestEU and the Innovation Fund, both in terms of directionality and funding. The recent Strategic Technologies for Europe Platform (STEP) is a starting point; however, it lacks financial capacity and replaces monetary support with signalling tools (e.g. the European Sovereign Seal). A proper federal fund – autonomous from the Commission – will administer European industrial policies.

Our two-tier structure rationalises a model to provide European public goods effectively, giving the EU a chance to increase prosperity and to craft a style of strategic autonomy that will not harm global dynamics. All in all, our proposal stresses the fundamental issue behind any European policy: an architecture, no matter how well-designed, won't work automatically; it needs resources. In other words: there will be no real strategic autonomy without real fiscal autonomy.