

Reindustrialising Europe: synergies of the Single Market

Michele Chang | Director of Transatlantic Affairs programme and Professor in the Department of European Political and Governance Studies at the College of Europe in Bruges | @michelemchang 

Theme

This policy paper offers guidelines for a European industrial policy that recognises the challenges faced by Europe and how solve them.

Abstract¹

The EU's [recent enthusiasm for industrial policy](#) in order to combat recent economic and strategic challenges sharply contrasts with its economic governance framework based on liberalisation and market discipline. Considering Europe's longer-term experience with industrial policy, one cannot take for granted its ultimate success, especially if it is pursued in isolation. This policy brief offers guidelines for the pursuit of a European industrial policy that recognises the challenges faced by Europe and how to best solve them. Specifically, the EU should continue to protect the single market and develop it further through [banking union](#) and capital markets union. While these solutions are not as novel as ideas for additional euro area financing, they are essential in order to ensure the long-term success of European reindustrialisation. National industrial policies risk fragmenting the single market, the prime source of influence for the EU. There is no political appetite for substantially increasing budgetary contributions to the EU, and reindustrialisation will require large-scale and sustained amounts of capital that can only be raised through markets.

In 2014 the Commission published a communication advocating a 'European Industrial Renaissance'. It proposed relatively modest aims compared to what we have witnessed recently. The Green Deal Industrial plan presented in February 2023 announced a scheme 'to provide a more supportive environment for the scaling up of the EU's manufacturing capacity for the net-zero technologies and products required to meet Europe's ambitious climate targets'.² The proposal was followed quickly with the Net Zero Industry Act and the Critical Raw Materials Act. Moreover, the proposed EU Chips Act (2022) also seeks to contribute to the green transition strengthening Europe's competitiveness and resilience in semiconductor technologies and applications. [The](#)

¹ This article is based on a presentation made at the Spanish Pre-Presidency Conference organized by the Elcano Royal Institute and TEPSA in Madrid (Spain) on 1 and 2 June 2023, <https://www.realinstitutoelcano.org/en/videos/spanish-pre-presidency-conference/>

² The Green Deal Industrial Plan (europa.eu), https://ec.europa.eu/commission/presscorner/detail/en/ip_23_510.

Spanish presidency lists 'the reindustrialisation of Europe' as a priority.³ The European Industrial Renaissance and the accompanying European industrial strategy appears to be in full swing.

This policy brief has three aims: (1) to explain the lessons from the previous attempts in Europe at industrial policy; (2) the reasons for the current interest in reviving industrial policy in Europe; and (3) policy prescriptions for moving forward. While the aforementioned acts to improve European competitiveness and reindustrialisation are significant, the EU lacks sufficient budgetary means to make a meaningful contribution to reindustrialisation. The private sector must also be harnessed through more concerted efforts at completing banking union and capital markets union in order to have the best possibility to reindustrialise Europe.

1. What is old is new again: Europe's previous forays into industrial policy

Industrial policy can be understood broadly as government support for industry. This can take different forms, such as government subsidies, guarantees, preferential financial conditions and other forms of protection for so-called 'national champions'. Countries like France and the UK attempted large-scale industrial policy in the post-WWII era as concerns over the gaps between Europe and the US, particularly in critical technology, led to European governments 'picking winners through sectoral policies, also defined as vertical industrial policies... aimed at sectors thought to be strategic and promising for the future' (Tagliapietra & Veugelers, 2020, p. 18), such as government support in computers and aerospace (Owen, 2012).

The US, however, enjoyed numerous advantages over Europe. First and foremost is its large single market and the consistent demand for high-tech products thanks to its military and space programmes. US support for such technology, therefore, goes well beyond specific industrial policies targeted towards an industry. In contrast, EU member States mostly resisted delegating authority to the EU (with some notable exceptions like the Airbus consortium), keeping industrial policy within national jurisdictions. Moreover, the deep and liquid capital markets in the US allowed for the involvement of private capital in technological innovation.

Europeans, as did the Americans, eventually became convinced of the advantages of market-based development rather than state-funded industrial policy, and in the 1980s European integration took a neoliberal turn. Markets, rather than governments, would pick winners and losers. The EU ensured a level playing field across Europe through its competition rules, especially those related to state aid, to prevent market distortions that would give an advantage to some companies over its competitors. Smith (2005, p. 316), dubbed the EU industrial policy developed during this period as 'competitiveness through competition'.

³ The president of the Government presents the priorities of the Spanish presidency of the Council of the EU (europa.eu), <https://spanish-presidency.consilium.europa.eu/en/news/priorities-of-the-spanish-presidency-of-the-council-of-the-eu/>.

This emphasis on strengthening competitiveness via market forces continued through a decade of economic crises in Europe. Neither the global financial crisis nor the euro crisis sought to overturn these principles, despite the temporary relaxation of state aid rules after the global financial crisis to support financial institutions through the Temporary Framework for State Aid (Lowe, 2009). [The euro crisis](#) led to a deep rift in the euro area as governments differed on the need for risk reduction versus risk sharing. The former prevailed as the northern European economies focused on the need for structural reforms in the peripheral economies to improve competitiveness. Competition Commissioner Joaquín Almunia (2012) reiterated years of EU policy when he declared that strict enforcement of EU competition rules was ‘the cheapest and most effective structural reform I can think of’. Market-based discipline remained the overriding principle of EU economic governance after a decade of crisis.

2. Understanding today’s industrial policy enthusiasm

In recent years, however, the EU has once again begun to contemplate what an IMF working paper referred to as a ‘return of the policy that shall not be named’ (Cherif & Hasanov, 2019). First, one can point to the economic changes that have occurred. The permacrisis in Europe since the global financial crisis has hampered economic growth and contributed to the decline of European manufacturing. In 2000 almost 27% of EU employment was in industry, falling to 22% by 2021. During the same period, employment in services rose from 65% to 73%. The EU is the top trader of services globally, with a surplus in trade in services in 2021 of €135 billion. Nevertheless, non-financial enterprises generated 48% of the total value added to the EU economy (Eurostat, 2022).

[The economic crisis caused by the pandemic](#) also exposed the lack of resilience of global supply chains, cutting Europe off from critical products like personal protective equipment, to name just one prominent example. The neoliberal policies that emphasised trade and competitiveness led to far-flung supply chains and dependence on third countries like China that could choose to cut off supply to critical products, leading to calls for greater European resilience. Indeed, the rise of China’s economy in the global trading system was accompanied by a massive industrial policy to support key sectors that has been estimated to range from 1.7% to 4.9% of China’s GDP (Glaser & Lee, 2023).

Moreover, the rise of industrial policy in economic rivals like the US has further emboldened proponents of industrial policy. The 2022 Inflation Reduction Act (IRA) in the US devotes US\$385 billion to energy and climate to accelerate its clean energy transition. While the EU has spent years encouraging the US to tackle climate change, it did not expect that it would do so with a policy that threatened European manufacturing through the mix of incentives offered by the US government.

Finally, while the economic implications of industrial policy loom large, they are dwarfed by their geostrategic implications. The 2022 US Chips and Science Act directs US\$280 billion in spending of which US\$52.7 billion will support semiconductor research, development, and manufacturing. In addition to enhancing US competitiveness, improving domestic semiconductor capacity also impacts national security. The EU

issued its own European Chips Act in 2022 with €43 billion to ensure supply resilience, joining other economies like China, Japan and South Korea in providing substantial support to the semiconductor industry. A ‘chip war’, particularly involving the US and China, contains important strategic implications given the role of chips in military technology (Miller, 2022).

3. The synergies of a European reindustrialisation

The EU’s industrial policy is an important pivot away from its previous market-oriented strategy. In addition, it occurs during a challenging economic period for the EU with high debt levels, the return of inflation and interest rate hikes. However, devoting substantial sums of money does not guarantee success in industrial policy. For example, Giesecke (2000) analyses the experience of the US and Germany in biotechnology. Despite both countries investing considerably in this sector, by the 1990s the US biotechnology sector had grown much larger than Germany’s.

In the EU’s response to initiatives like the IRA, it needs to think more broadly than protecting the competitiveness of European industries (Kleimann *et al.*, 2023). Indeed, the EU must consider the synergies between its burgeoning industrial policy and other policy programmes. Without the success of the single market more generally and financial integration (via banking union and capital markets union) more specifically, the amounts pledged by the EU thus far would be too modest to achieve its objectives. Given the inherently risky nature of industrial policy, there are two broad guidelines that the EU should follow as it develops its industrial policy.

3.1. Support the single market

At the 2022 State of the European Union address, Commission President Ursula von der Leyen pledged, ‘I will push to create a new European Sovereignty Fund. Let’s make sure that the future of industry is made in Europe’.⁴ Indeed, a supranational budget would mitigate the kinds of distortions that national state aid would bring, as this is correlated with national fiscal resources that favour larger member states. While analysts have supported calls for a centralised fiscal capacity as part of a European industrial strategy (Steinberg & Otero Iglesias, 2023), northern member States have been sceptical about a fresh influx of cash into EU coffers. Dutch Prime Minister Mark Rutte noted after a meeting with French President Emmanuel Macron, ‘We have agreed to first look closely at the funds already available in the EU’.⁵ In June 2023 the Commission’s European Sovereignty Fund had become the Strategic Technologies for Europe Platform (STEP).⁶ Far from a repeat of Next Generation EU (NGEU) budget, STEP reallocates existing money along with a request for an additional €10 billion from member States.

⁴ SOTEU_2022_Address_EN.pdf (europa.eu), https://state-of-the-union.ec.europa.eu/system/files/2023-06/SOTEU_2022_Address_EN.pdf.

⁵ France, Netherlands agree on ways EU could deal with U.S. state aid, Dutch PM says | Reuters, <https://www.reuters.com/world/france-netherlands-agree-ways-eu-could-deal-with-us-state-aid-dutch-pm-says-2023-01-30/>.

⁶ EU budget (europa.eu), https://ec.europa.eu/commission/presscorner/detail/en/ip_23_3364.

The generosity and solidarity of EU member States during the COVID-19 crisis that resulted in the NGEU budget is unlikely to be repeated soon. Another scheme could be developed with the European Investment Bank similar to the European Fund for Strategic Investment that offered loan guarantee that promised to trigger additional private investment and was succeeded by InvestEU. Nevertheless, it likely would fall short of what is required, given the scale of investment needed across Europe.

Some have argued for a relaxation of EU state aid rules, and even ‘a European regulatory pause’ on environmental regulation was proposed by Macron in May 2023⁷ to allow for a more rapid European reindustrialisation. This risks fragmenting the single market, as not all member States possess the same resources to allocate to industrial policy. For example, in order to support member States’ economies in the aftermath of Russia’s invasion of Ukraine, in March 2022 the Commission adopted the Temporary Crisis and Transition Framework that includes some ‘limited amounts of state aid, liquidity support in form of State guarantees and subsidised loans, (and) aid to compensate for high energy prices’.⁸ Under this framework, €672 billion of state aid has been granted, over half of it in Germany and almost a quarter in France. This illustrates the conundrum in which larger member States have more fiscal space for state aid, presenting a serious risk to the single market. Allowing for ever more state aid would ‘threaten to undermine the Single Market, the EU’s greatest success, and to widen the gulf between richer and poorer EU members’ (Holzhausen, 2023, p. 1).

3.2. Spread the costs and the risks with financial integration

Proposals for a banking union (2012) and capital markets union (2014) sought to address the fragmented nature of the European financial system. This had contributed to the famous doom loop or ‘vicious circle’ (Euro Area, 2012) between heavily indebted sovereigns and weak banks that fuelled speculation during the euro crisis. Banking Union (BU) became operational in 2014 as European Central Bank became the supervisor for euro area banks (and non-euro area banks with ‘close cooperation’ status) as the Single Supervisory Mechanism. The Single Resolution Mechanism regulation entered into force that same year.

Commission President Jean-Claude Juncker launched plans for a Capital Markets Union (CMU) in a speech on 6 November 2014. He opened this speech by saying that his mandate and the CMU launch would be defined by: ‘How to kick-start growth. How to bring together public and private funding. How to increase the options businesses have for their financing. And how to get our economies back on track for the longer term’ (Juncker, 2014). Moreover, it was expected that both BU and CMU would improve the stability of the European financial system and foster integration that would open up new financing opportunities for business.

⁷ Macron calls for ‘regulatory break’ in EU green laws to help industry – EURACTIV.com, <https://www.euractiv.com/section/energy-environment/news/macron-calls-for-regulatory-break-in-eu-green-laws-to-help-industry/>.

⁸ Temporary Crisis and Transition Framework (europa.eu), https://ec.europa.eu/commission/presscorner/detail/en/ip_23_1563.

Nearly a decade has passed, and neither has progressed substantially due to reluctant member States and their national supervisors wishing to hang on to control over these economically and politically significant areas (Högenauer, Howarth & Quaglia, 2023; Piroska & Epstein, 2023). Banking Union's third pillar of European deposit insurance has been stalled since its 2015 proposal, and the European Parliament and the Council only reached a political agreement on the 2021 Commission proposal known as the 'banking package' that would implement the Basel III standards in June 2023.⁹ Meanwhile, progress on capital markets union has been slow. Recent measures include the listing act package that would ease the administrative burden of listing on European stock markets.¹⁰

Successive European Council and Euro Summit statements have urged for CMU's development, and in March 2023 the Presidents of the European Council, European Commission, Eurogroup, European Central Bank and European Investment Bank noted that 'we have been too slow for too long on one essential building block: the Capital Markets Union... this includes more aligned insolvency laws... and more integrated capital markets supervision'.¹¹ While BU and CMU share similar sounding names, they are very different as the former is substantially more integrated than the latter. And while common or aligned insolvency laws and supervision would be essential components of an integrated European capital market, the current state of CMU is a long way from this. Nevertheless, it is an important and welcome development that these leaders have identified publicly these as being (ultimate) objectives of CMU. Delegating further supervisory tasks and competences to the European Securities and Markets Authority would be a good step towards a genuine CMU.

Eurogroup President Paschal Donohoe announced that the Eurogroup 'set ourselves the aim of reaching agreement by March 2024 on areas we would like to ask the next Commission to consider with a view to deepening the capital markets union. This means giving strategic consideration to areas in which further progress is possible and likely in the years ahead'.¹² There is no time to lose.

Conclusions

Europe is undergoing a major pivot from its policies that had emphasised liberalisation and market forces. Geopolitical and economic challenges now clash with governments faced with high debt levels accumulated during the COVID-19 crisis. Despite the impressive solidarity shown in 2020, the scepticism of northern European economies

⁹ Commission welcomes political agreement on EU Banking Package (europa.eu), https://finance.ec.europa.eu/news/commission-welcomes-political-agreement-eu-banking-package-2023-06-27_en.

¹⁰ Capital markets union: Council agrees its negotiating mandate on the listing act - Consilium (europa.eu), <https://www.consilium.europa.eu/en/press/press-releases/2023/06/14/capital-markets-union-council-agrees-its-negotiating-mandate-on-the-listing-act/>.

¹¹ 'Channeling Europe's savings into growth' - Op-ed article by European Council, European Commission, Eurogroup, ECB and EIB Presidents - Consilium (europa.eu), <https://www.consilium.europa.eu/en/press/press-releases/2023/03/09/channeling-europe-s-savings-into-growth-op-ed-article-by-european-council-european-commission-eurogroup-ecb-and-eib-presidents/>.

¹² Timeline - Capital markets union - Consilium (europa.eu), <https://www.consilium.europa.eu/en/policies/capital-markets-union/timeline-capital-markets-union/>.

towards further risk sharing has not abated. A fresh influx of cash to support European reindustrialisation likely will not be forthcoming, though it may be an optimal, albeit partial, solution. If reindustrialisation is to succeed, however, this will not include the fragmentation of the single market through the relaxation of state aid rules to allow for national industrial policies. Moreover, the most lasting and effective change would be progress on banking union and capital markets union. Reindustrialisation requires a realistic assessment of how to fund it over the longer term, and an effective single market bolstered by integrated financial markets are needed.

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