

REPORT & RECOMMENDATIONS

12th Meeting (virtual)

Trade policy in the context of the US Inflation Reduction Act and the EU Green Industrial Plan

7 March 2023

At the request of the chairman, Mr John Bruton, the executive director of the HLGs, Stefan Schepers, welcomed the members¹ and chaired meeting. This time their brainstorming would focus on the importance of the multilateral rules-based system and free trade to ensure the competitiveness of the European Single Market against a background of increasing geopolitical challenges and protectionist intervention as exemplified by the US Inflation Reduction Act.

For more than ten years now, the working method has aimed for an ‘open innovation’ approach between governments, business and academia, to inject innovative policy ideas into the EU system. It results from an initiative in the Competitiveness Council.²

1

RECOMMENDATIONS

Following this brainstorming, the HLG on Trade Policy Innovation proposes the following:

- The HLG recommends to avoid a subsidy competition between the EU and the US. Instead, the EU should engage with the US as equals, emphasising mutual interests and shared values in the current geopolitical context.
- Therefore, HLG recommends making use of existing instruments in the EU’s legal and political framework to defend the validity of the multilateral rules-based system of WTO.
- However, opening a pathway to reform and strengthen the WTO should be considered in order to design a set of basic rules that are better acceptable by all countries.

¹ Members participate in their personal capacity. All recommendations for action and all ideas for further consideration have not always been agreed on by all members, but advice is based on a very wide consensus. The final version is written under responsibility of the chairman and the executive director

² Competitiveness Council, 5-6 December 2011, Presidency Note.

Trade Policy Innovation

- In parallel, the EU should finalise Free Trade Agreements with various countries and regions. Therefore, it is important to take into account their views and needs, avoid Eurocentrism and avoid applying a “one size fits all” approach.
- The HLG highlights the importance of trade as an integral part of Europe’s strategic autonomy. The EU/EEAS policy needs to be strategically linked to its ambition for greater autonomy and resilience. The EU Green Industrial Act should be embedded in a more holistic and synergetic approach to external and trade policy.
- The HLG recommends boosting the European competitiveness by strengthening the EU Single Market and its level-playing field. For this, the HLG recommends :
 - A rapid and consistent effort of simplification of regulations and coherence between them;
 - Recognising and reinforcing the role of SMEs and start-ups in the global scenario;
 - Improved engagement by EU policy-makers with businesses including proper and user-friendly consultations about the appropriate tools to achieve public interest objectives while facilitating their competitiveness.
- The HLG underscores the importance of having skilled workforce in the European industry and recommends avoiding labour market mismatches.
- The HLG recommends improving communication on the benefits of trade which is often neglected by policy-makers which results in misunderstandings by society on trade policy.
- The HLG recommends strengthening the capacities of EU trade officials and EEAS diplomats to help them deal with the heightened political risk in key supply chains and to develop a consistent EU trade and industrial policy in a challenging scenario.
- Overall, the HLG recommends improving cooperation, coordination and synergies between the tasks of the DGs, EU delegations and agencies, and the EEAS, to develop a EU trade policy more coherent with internal and external objectives.

SUMMARY OF DISCUSSIONS

The weaponization of trade understood as the use of trade as a strategic tool to gain advantage around the world is gaining a momentum in geopolitics³. The use of trade as a coercive tool to achieve political goals and geopolitical ambitions is not new. What is different, is the extent to which trade is being integrated into the military and defence strategies of major powers such as the United States, China and Russia.

³ Harding, R., & Harding, J. (2017). *The weaponization of trade: The great unbalancing of politics and economics*. London Publishing Partnership.

Trade Policy Innovation

The post-II World War Western world, which witnessed the creation of the GATT (that would become the WTO), was marked by a trend towards more free trade, inspired by the premises of economic liberalism and multilateralism. This permitted the production of unprecedented prosperity and wealth among nations.

Now the context has changed and trade has to evolve in a new geopolitical context. The post-war order is disintegrating because the interests of new powers do not automatically coincide with a system designed by the West, because of the emergence of new technologies and new challenges, such as global health or climate change.

A new approach to trade, adapted to the new world order, is needed and requires new policy frameworks. These new concepts should be strategic and operational but also more inclusive. European prosperity depends on a stable world order, and this depends on taking into account, evidence-based and with foresight, the interests of others.

(1) The importance of Trade in an era of shifting geopolitics

The US Inflation Reduction Act is a sign of the times and reflects the geopolitical dimensions of trade: the US feels it must act in the face of the perceived threat from China which operates a different economic system. Europeans' biggest concern about the US Inflation Reduction Act is the "Make it in America" provisions for the use of US-made clean energy equipment by subsidising, for example, US-made electric cars, solar panels and batteries.

A study of the US Inflation Reduction Act and its impact is not yet possible as it depends on future technologies and their impact. What can be said, however, is that it is unlikely that many companies will migrate to the US. Moving to another country does not depend on just a subsidy; several factors are decisive. What is certain is that companies that are already in the US will invest more there.

Structurally high energy prices in Europe are however concerning: if this continues, it will have an impact. Nevertheless, Europe should not go on a subsidy competition because of this. Instead, Europe should engage with the US and seek a dialogue in order to keep close relations and secure those of our interests which can be shared.

Resilience will improve if the state/EU intervenes appropriately in the economy and moves from a short-term and internal to a medium and long-term and international perspective. Strategic autonomy includes elements of engaging with the outside world and shaping it for mutual benefit.

Until now, Europe has focused a lot on sustainability but a shift towards more concern for competitiveness is needed.

Trade Policy Innovation

Trade is a powerful instrument for wealth creation and the renationalisation of trade is dangerous. Fair trade can be also seen as a developing instrument, for example in Africa. Therefore, Europe needs to take into account the necessities of our partners and not apply a one-size fits it all approach.

The changing global order will affect the African-European relations on several dimensions. In 'a world of more equal partnerships between regional blocs', Europe's relative importance is declining. In this context, seeking a real partnership with Africa (while also competing with other players such as US, China, Russia or India) is not limited to the economic sphere but also has a geopolitical dimension.

(2) Strengthening the multilateral rules-based system and communicating on its benefits

The multilateral free trade system based on rules and whose institutional cornerstone is the WTO provides tangible economic and social benefits to states and societies. This is why it should be preserved.

The EU is in favour of the multilateral order based on the WTO. If the US subsidies harm EU interests, a complaint to the WTO should be considered. This would send an unmistakable political signal that the EU remains invested in the WTO's rules-based system, values the balance of concessions codified in the WTO agreements, holds the US accountable for breaches of its commitments and seeks leverage for future bilateral negotiations with US trade representatives.

To ensure compliance with WTO rules, consideration should be given to **reforming the WTO** to find a set of rules that are accepted by all.

Europe needs to employ other ways of cooperation and to ratify **Free Trade Agreements** with various countries to materialise ongoing dialogues with New Zealand, Australia, India, Chile, Mexico, Mercosur, etc.

Free Trade Agreements are part of the solution, but the WTO must be the cornerstone of the system. Most trade conducted by European countries is still done under the WTO Most-favoured-nation system. Rules are needed and it is in the interest of the EU to protect and strengthen the rules-based system, even if there is a risk that the EU alone will stick to this system and will have trading partners that do not believe in this system, e.g. the US or China.

The benefits of trade and trade policy need to be explained to citizens. Sometimes the profits of trade are neglected by the trade experts involved. It is the job of politicians to communicate the benefits of free trade and find a way to show them. Too often only the costs of trade are seen.

The EU should be proud and communicate about its achievements, e.g. that the Single Market is an advantage, a leverage and needs to be better explained to the society in the EU.

Trade Policy Innovation

(3) Stimulating the European economy and competitiveness

The emerging geopolitical changes necessitate a deeper discussion to contribute to reforms aimed at maintaining and improving Europe's competitiveness in the face of an increasingly challenging global scenario. An effective Union response has both an internal and an external dimension. **Europe should not seek to copy the US Inflation Reduction Act** and follow the American way: Europe and the US are different; Europe has its own tools and trade defence instruments; Europe has its own strengths.

The biggest financial burden for companies is not the energy crisis and prices, but bureaucracy, of both EU and national and even regional origin. There is a need for the **simplification of regulations** that already exist and synergy between them. This does not mean deregulation. Digitalisation and consultation with the destinies of the regulation need to improve.

Better impact assessments and a reform of the methods and culture in the European system, as not only the Commission but also the working groups in the Council and Parliament are responsible for the regulatory confusion.

SMEs suffer from geopolitical tensions in trade as their needs are often overlooked in trade policy and negotiations. So do start-up companies which are often future industrial champions. Over the course of the last few decades, the EU has been a “follower” rather than a leader in the development of start-up companies. This is even more evident in the digital economy, where start-up companies experience the EU single-market fragmentation, regulatory burdens, or limited access to capital, incomplete research area. The EU should be ready now to effectively implement a series of actions which can support the development of an ecosystem in which companies can thrive and do not feel the necessity to seek support for upscaling outside the EU.

EU policy-makers need **more engagement with business**, through private hearings and public consultations.

In addition, a stronger **dialogue between the different DGs** should be established. Beyond DG Trade other DGs should be involved in shaping European trade policy. The politicisation of trade has already been underway for ten years. However, Europe has just realised the economic importance of geopolitical investments. Foreign policy needs to be more strategically linked to the EU's trade policy.

Moreover, the Commission should take a more **holistic approach to trade**: an overall picture rather than fragmented measures or a purely legalistic view is now needed. A broader agenda that takes into account all relevant internal and external policies is necessary.

The Commission should not be a scapegoat, because the regulatory burden has more sources besides the Commission : the Council and Parliament, which operate without proper impact assessment, and the member states. They all must become more conscious of the impact of their policy decisions.

Trade Policy Innovation

Securing and strengthening a fully functioning **Single Market is key to competitiveness**. The Single Market is a trade asset as well as a key source of prosperity for the people of Europe. The level playing field of the internal market is at risk after trillions of euros in state subsidies were approved during the pandemic and to deal with the initial shock caused by Russia's invasion of Ukraine.

The EU Green Deal Industrial Plan is intended to pave the way for European industry to become a global leader in the climate neutral transition. In order to achieve this, it is crucial to have a **skilled workforce** and to avoid mismatches in the labour market and to make the research to production and market chain more flexible and fast.

The EU should keep an **updated foresight and mapping of the capabilities for crisis management** within the European Commission, in the EEAS and in its agencies. It should make critical supply chains more diverse and reduce dependencies on single regions and/or producers to mitigate shortages and delays of supplies. In addition, schemes should be defined for fast allocation of emergency research funding to trigger rapid research development to solve aspects of the crisis. All this would strengthen European competitiveness.

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